Notices to Members

August 1999

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NASD®
Parent of The Nasdaq-Amex Market Group

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NOTE: As of January 1999, there has been a change in *Notices to Members* distribution: Members no longer receive complimentary copies of *Notices to Members*. Each Executive Representative is entitled to one annual subscription at cost ($15 per year). Additional annual subscriptions are available for $225; single issues cost $25. Send a check or money order (payable to the National Association of Securities Dealers, Inc.) to NASD MediaSource, P.O. Box 9403, Gaithersburg, MD 20898-9403, or to phone in an order using American Express, MasterCard, or Visa charge, call (301) 590-6142, Monday to Friday, 9 a.m. to 5 p.m., Eastern Time. Back issues may be ordered by calling MediaSource at (301) 590-6142.

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

NASD Notice to Members 99-63

SEC Approves And Adopts Revised Forms And Electronic Filing Requirement; New Member Applicants Should Continue To File Paper Forms

Suggested Routing

- ■ Senior Management
- ☐ Advertising
- ☐ Continuing Education
- ☐ Corporate Finance
- ☐ Executive Representatives
- ☐ Government Securities
- ☐ Institutional
- ☐ Insurance
- ☐ Internal Audit
- ■ Legal & Compliance
- ☐ Municipal
- ☐ Mutual Fund
- ■ Operations
- ☐ Options
- ■ Registered Representatives
- ■ Registration
- ☐ Research
- ☐ Syndicate
- ■ Systems
- ☐ Trading
- ☐ Training
- ☐ Variable Contracts

Executive Summary

The Securities and Exchange Commission (SEC) has approved revised Forms U-4 and U-5 and adopted revised Forms BD and BDW[1], all of which will be effective August 1, 1999. The SEC also approved amendments to National Association of Securities Dealers, Inc. (NASD®) Rule 1140—the Electronic Filing Rule—which requires such Forms (with the exception of initial Form BD applications) to be filed electronically, effective August 16, 1999. For details on the transition to electronic Forms and filings, see *Notice to Members 99-56* and visit the Web CRD Internet Page at *www.nasdr.com/3400_web.htm*.

New member applicants should continue to file Forms BD and U-4 on paper according to NASD Rule 1013.

Questions concerning this *Notice* may be directed to Ann E. Bushey, Assistant Director, CRD/Public Disclosure, NASD Regulation, Inc. (NASD Regulation®) at (301) 590-6389; Mary M. Dunbar, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8252; or Richard E. Pullano, Associate Director and Counsel, CRD/Public Disclosure, NASD Regulation, at (301) 212-3789.

Background And Discussion

In *Notice to Members 99-56*, NASD Regulation describes the scheduled August 1999 deployment of the new Internet-based Central Registration Depository system, Web CRD℠. As anticipated in that *Notice*, the SEC has approved the revised Forms U-4 and U-5 and adopted revised Forms BD and BDW for use with Web CRD.[2] On August 1, 1999, all of these new Forms become effective, and the Interim Forms currently in use become obsolete.

The SEC also has approved amendments to the Electronic Filing Rule which become effective August 16, 1999.[3] The entire text of the amended Rule appears in Attachment A.

Paper Filing For New Member Applicants

New member applicants should continue to file paper Forms BD and U-4 under NASD Rule 1013. New member applicants may use paper Interim Forms BD and U-4 until July 29, 1999; **however, such Interim Forms must be received by NASD Regulation by close of business July 29**. Beginning on August 1, 1999, new member applicants should download the new Forms BD and U-4 from NASD Regulation's Web Site at *www.nasdr.com* and submit them in paper to CRD.[4] CRD will then establish an electronic account that will allow new member applicants to submit all subsequent filings electronically. In the future, NASD Regulation may amend its rules to require new member applicants to file all Forms electronically.

See *Notice to Members 99-56* for more details on the transition to Web CRD and Securities Exchange Act Release No. 41594 for details on the adoption of revised Form BD. Visit the Web CRD Internet Page at: *www.nasdr.com/3400_web.htm* for all of the latest developments on the deployment of the new system.

Attachment A

Following is the entire text of revised Rule 1140.

1140. Electronic Filing Rules

(a) Filing Requirement

All forms required to be filed by Article IV, Sections 1, 7, and 8, and Article V, Sections 2 and 3, of the By-Laws shall be filed through an electronic process or such other process the Association may prescribe to the Central Registration Depository.

(b) Supervisory Requirements

(1) In order to comply with the supervisory procedures requirement in Rule 3010, each member shall identify a Registered Principal(s) or corporate officer(s) who has a position of authority over registration functions, to be responsible for supervising the electronic filing of appropriate forms pursuant to this Rule.

(2) The Registered Principal(s) or corporate officer(s) who has or have the responsibility to review and approve the forms filed pursuant to this Rule shall be required to acknowledge, electronically, that he/she is filing this information on behalf of the member and the member's associated persons.

(c) Form U-4 Filing Requirements

(1) Initial and transfer electronic application filings shall be based on a signed Form U-4 provided to the member by the applicant. As part of the member's recordkeeping requirements, it shall retain the applicant's signed Form U-4 and make it available upon regulatory request.

(2) Fingerprint Cards

Upon filing an electronic Form U-4 on behalf of an applicant for registration, a member shall promptly submit a fingerprint card for the applicant. NASD Regulation may make a registration effective pending receipt of the fingerprint card. If a member fails to submit a fingerprint card within 30 days after NASD Regulation receives the electronic Form U-4, the person's registration shall be deemed inactive. In such case, NASD Regulation shall notify the member that the person must immediately cease all activities requiring registration and is prohibited from performing any duties and functioning in any capacity requiring registration. NASD Regulation shall administratively terminate a registration that is inactive for a period of two years. A person whose registration is administratively terminated may reactivate the registration only by reapplying for registration and meeting the qualification requirements of the applicable provisions of the Rule 1020 Series and the Rule 1030 Series. Upon application and a showing of good cause, the Association may extend the 30-day period.

(d) Form U-5 Filing Requirements

Initial filings and amendments of Form U-5 shall be submitted electronically. As part of the member's recordkeeping requirements, it shall make such records available upon regulatory request.

(e) Third Party Filing

A member may employ a third party to file the required forms electronically on its behalf.

Endnotes

[1]Forms BD and BDW are joint forms used by the SEC, self-regulatory organizations (SROs), and the states. The forms are used, respectively, to register, and to terminate the registration of, broker/dealers. SROs and the states use Forms U-4 and U-5 to register, and terminate the registration of, associated persons of broker/dealers.

[2]See Exchange Act Rel. Nos. 41356 (April 30, 1999), 41560 (June 25, 1999), and 41594 (July 2, 1999).

[3]See Exchange Act Rel. No. 41575 (June 29, 1999).

[4]NASD Regulation will accept new Forms BD and U-4 during the System Transition Period; however, NASD Regulation will not enter these Forms into Web CRD until August 16.

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This *Special Notice to Members* was mailed to members on August 4, 1999.

Special NASD Notice to Members 99-64

NASD Informs Members Of Upcoming Nomination Procedures For Industry Member Vacancies On The National Adjudicatory Council

Suggested Routing

- ■ Senior Management
- ☐ Advertising
- ☐ Continuing Education
- ☐ Corporate Finance
- ☐ Executive Representatives
- ☐ Government Securities
- ☐ Institutional
- ☐ Insurance
- ☐ Internal Audit
- ■ Legal & Compliance
- ☐ Municipal
- ☐ Mutual Fund
- ☐ Operations
- ☐ Options
- ☐ Registered Representatives
- ☐ Registration
- ☐ Research
- ☐ Syndicate
- ☐ Systems
- ☐ Trading
- ☐ Training
- ☐ Variable Contracts

Executive Summary

The purpose of this *Special Notice to Members* is to advise members of the nomination procedures to fill upcoming vacancies on the National Adjudicatory Council (NAC). The terms of NAC members from the West Region and New York City are expiring in January 2000.

Members are encouraged to submit names of candidates to the appropriate Regional Nominating Committee Chairs (listed in Exhibit I), the NASDR℠ District Director (listed in Exhibit I), or National Association of Securities Dealers, Inc. (NASD®) Corporate Secretary Joan Conley by September 1, 1999. The Chair or a District Director in the Region will provide each nominee with a biographical form for completion. The completed form will be provided to all Regional Nominating Committee members for review. On or about October 1, 1999, the Regional Nominating Committees will provide members with written notice of NAC candidates.

Current Industry members of the NAC and their terms are listed in Exhibit I. The procedures to fill the NAC vacancies are outlined in Exhibit II. Questions concerning this *Special Notice to Members* may be directed to the District Directors in the Region noted or to Joan C. Conley, Corporate Secretary, NASD, at (202) 728-8381.

National Adjudicatory Council Membership And Function

Membership

The NAC consists of 12 members—six Industry members and six Non-Industry members. Five Industry members each represent one of the following geographic regions and the sixth Industry member is selected at large.

West Region: Hawaii, California, Nevada, Arizona, Colorado, New Mexico, Utah, Wyoming, Alaska, Idaho, Montana, Oregon, and Washington.

South Region: Alabama, Arkansas, Kentucky, Louisiana, Mississippi, Oklahoma, Tennessee, Texas, Florida, Georgia, North Carolina, South Carolina, Puerto Rico, Virginia, Canal Zone, and the Virgin Islands.

Central Region: Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, Illinois, Indiana, Michigan, and Wisconsin.

North Region: Delaware, Maryland, Pennsylvania, West Virginia, District of Columbia, New Jersey, Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island, Vermont, and New York (except for New York City).

New York: New York City.

Function

According to the NASD By-Laws, the NAC is authorized to act for the NASD Board of Governors in matters concerning:

- an appeal or review of a disciplinary proceeding, a statutory disqualification proceeding, or a membership proceeding;
- a review of an offer of settlement; a letter of acceptance, waiver, and consent; and a minor rule violation plan letter;
- the exercise of exemptive authority;
- and such other proceeding or actions authorized by the Rules of the Association.

The NAC also shall consider and make recommendations to the Board on policy and rule changes relating to the business and sales practices of NASD members and associated persons and enforcement policies, including policies regarding fines and other sanctions.

EXHIBIT I
1999 National Adjudicatory Council Industry Members

West Region
Districts 1, 2, 3a, and 3b

NAC Industry Member	Term Expiration
Nicholas C. Cochran American Investors Company	January 2000

NASD members are encouraged to submit names of candidates for this NAC member seat. Please submit candidates' names to any of the following:

Joan B. Seidel, Regional Nominating Committee Chair
Morton Seidel & Company, Inc.
8730 Wilshire Blvd., Suite 530
Beverly Hills, CA 90211
(310) 360-7541

Elisabeth P. Owens, District 1 Director
525 Market Street, Suite 300
San Francisco, CA 94105
(415) 882-1200

Lani M. Sen Woltmann, District 2 Director
300 South Grand Avenue, Suite 1600
Los Angeles, CA 90071
(213) 627-2122

Frank J. Birgfeld, District 3a Director
Republic Plaza Building
370 17th Street, Suite 2900
Denver, CO 80202-5629
(303) 446-3100

James G. Dawson, District 3b Director
Two Union Square
601 Union Street, Suite 1616
Seattle, WA 98101-2327
(206) 624-0790

Joan Conley, NASD Corporate Secretary
1735 K Street NW
Washington, D.C. 20006
(202) 728-8381

South Region
Districts 5, 6, and 7

NAC Industry Member	Term Expiration
Raymond E. Wooldridge Southwest Securities, Inc.	January 2001

Central Region
Districts 4, 8a, and 8b

NAC Industry Member	Term Expiration
Ronald D. Brooks Banc One Capital Markets, Inc.	January 2001

North Region
Districts 9a, 9b, and 11

NAC Industry Member	Term Expiration
Richard J. DeAgazio Boston Capital Services, Inc.	January 2001

New York
District 10

NAC Industry Member	Term Expiration
David DeMuro Lehman Brothers, Inc.	January 2000

NASD members are encouraged to submit names of candidates for this NAC member seat. Please submit candidates' names to any of the following:

Joan Caridi, Regional Nominating Committee Chair
Citigroup, Inc.
425 Park Ave., 3rd Floor
New York, New York 10043
(212) 793-7181

David Leibowitz, District 10 Director
NASD Financial Center
33 Whitehall Street
New York, NY 10004
(212) 858-4000

Joan Conley, NASD Corporate Secretary
1735 K Street NW
Washington, D.C. 20006
(202) 728-8381

At Large NAC Industry Member

NAC Industry Member	Term Expiration
Theodore A. Levine PaineWebber Group, Inc.	January 2000

EXHIBIT II

1999 National Adjudicatory Council Nomination Procedures

1. NASD Regulation maintains Regional Nominating Committees in the manner specified in Article VI of the By-Laws of NASD Regulation, Inc.

2. Members located in the West Region and New York City are hereby notified of the upcoming election of members to the National Adjudicatory Council and are encouraged to submit names of potential candidates to their respective Chair of the Regional Nominating Committee, District Director (see Exhibit I), or to NASD Corporate Secretary Joan Conley by September 1, 1999.

3. Nominees will be asked to complete a biographical form which will be reviewed by the Regional Nominating Committee.

4. The Regional Nominating Committee shall review the background of the candidates and the description of the NASD membership provided by NASD Regulation staff and shall propose one or more candidates for nomination to the National Nominating Committee on or before September 24, 1999. In proposing a candidate for nomination, the Regional Nominating Committee shall endeavor to secure appropriate and fair representation of the region.

5. On or before October 1, 1999, the Regional Nominating Committee shall notify in writing the Executive Representatives and branch offices of the NASD members in the region the name(s) of the candidate(s) proposed for nomination to the National Adjudicatory Council.

6. If an officer, director, or employee of an NASD member in the region is not proposed for nomination by the Regional Nominating Committee and wants to seek the nomination, he or she shall send a written notice to the Regional Nominating Committee Chair or the Secretary of NASD Regulation within 14 calendar days after the mailing date of the Regional Nominating Committee's notice (#5 above) and proceed in accordance with the Contested Nomination Procedures found in Article VI of the NASDR By-Laws.

7. If no additional candidate comes forward within 14 calendar days, the Regional Nominating Committees shall certify their candidates to the National Nominating Committee.

Additional information pertaining to the District Election Procedures can be found in Article VI of the By-Laws of NASD Regulation. The By-Laws can be found in the on-line *NASD Manual* at *www.nasdr.com*.

NASD Notice to Members 99-65

SEC Approves Rule Changes To NASD Trade-Reporting Rules For Riskless Principal Transaction In Nasdaq And OTC Securities

Suggested Routing

- ■ Senior Management
- □ Advertising
- ■ Continuing Education
- □ Corporate Finance
- □ Executive Representatives
- □ Government Securities
- ■ Institutional
- □ Insurance
- □ Internal Audit
- ■ Legal & Compliance
- □ Municipal
- □ Mutual Fund
- ■ Operations
- □ Options
- □ Registered Representatives
- □ Registration
- □ Research
- □ Syndicate
- ■ Systems
- ■ Trading
- ■ Training
- □ Variable Contracts

Executive Summary

On March 24, 1999, the Securities and Exchange Commission (SEC) approved amendments to National Association of Securities Dealers, Inc. (NASD® or Association) rules regarding trade reporting of riskless principal transactions by Market Makers. The rule change will permit Market Makers in Nasdaq® and other over-the-counter securities to report trades under the current riskless principal rules that exist for non-Market Makers. The effect of the change is that instead of reporting both "legs" of a riskless principal transaction, Market Makers (like non-Market Makers currently) now will only report one portion of the transaction if it meets the definition of riskless principal. The rule defines riskless principal as a trade in which a member, after having received an order to buy (sell) a security, buys (sells) the security at the same price, as principal, in order to satisfy the order to buy (sell).

This *Notice* includes questions and answers regarding the rule changes (Attachment A); and the text of the rule changes (Attachment B). These changes are effective as of September 30, 1999.

Questions/Further Information

Questions concerning this *Notice* may be directed to the Office of General Counsel, The Nasdaq Stock Market, Inc., at (202) 728-8294; or Market Regulation Legal Section, NASD Regulation, Inc. (NASD Regulation®), at (301) 590-6410.

Background

The rules for reporting trades in Nasdaq securities have long existed in their current form. The rules were broadly designed to capture all trading activity by broker/dealers, both dealer-to-dealer trades and trades with customers. These rules, and the trade reports that result, serve several important purposes. They form the basis for public dissemination of "last sale" transaction prices to the tape, thus providing transparency. Trade reports also are an integral part of the audit trail used by the NASD in its regulatory efforts to surveil and regulate firms' activities. Given the historical structure of the dealer markets and the need to provide a comprehensive view of all trading, and because Market Makers were always deemed to be "at risk" when trading from their principal accounts, NASD trade-reporting rules have required the reporting of all principal trades by Market Makers.

Non-Market Makers, however, generally do not report all principal trades under current rules, to the extent the trades are defined as "riskless" — that is, they involve a trade with another member, usually a Market Maker, which is used to offset a trade with a customer. This riskless principal exception to the general rule of reporting all principal trades results in one trade report even though the non-Market Maker firm is involved in two separate trades against its principal account.

In light of the growth and evolution of the structure of Nasdaq and the over-the-counter (OTC) market, the NASD is now extending the riskless principal exception to Market Makers in Nasdaq-listed securities (including Nasdaq convertible debt securities) as well as other securities traded over-the-counter (*e.g.*, OTCBB and pink sheets). Thus, certain matching principal trades involving a Market Maker are now explicitly included within the riskless definition, and reported to the public tape only once. For example, under the SEC Order Handling Rules, Nasdaq Market Makers now display customer limit orders in their public quotes. Those

orders are often filled by the Market Maker when that quote is accessed by another market participant.[1] Because Market Makers generally trade exclusively from a principal account, it is necessary to engage in two separate principal trades: one with the other market participant, and then another directly with the customer. Both of these trades are reported by Market Makers under current rules. In effect, however, these two trades can be viewed as one event – the execution of a customer order upon the execution of an offsetting transaction obtained by the Market Maker. Under the proposed rule change, these two trades are reported only once. One of the expected benefits of the extension of riskless principal trade reporting to Nasdaq and OTC Market Makers is the reduction of SEC transaction fees, which generally are assessed to the seller in a transaction that is trade reported.

The new rules define "riskless principal" as a trade in which a member, after having received an order to buy (sell) a security, buys (sells) the security at the same price, as principal, in order to satisfy the order to buy (sell). In order to qualify for riskless principal trade reporting, the rule requires that the trades be executed at the "same price" (exclusive of a markup or markdown, commission equivalent, or other fee). Additionally, under the rules a portion of a transaction may be deemed riskless. That is, to the extent that any of the order is offset with another principal execution at the same price, that portion is deemed riskless and should be reported only once.

In addition, the NASD has made certain technical changes to the existing rule. Specifically, while the current rule refers to orders received from a "customer", the new rule simply refers to "an order." This change ensures consistent application of the riskless principal trade-reporting rules to any order received by a member, regardless of the person or entity from whom it was received. Furthermore, the NASD has amended the rules to more clearly provide that riskless principal trades are reported exclusive of any fee, not just markups and markdowns.

Attachment A – Questions And Answers

General Questions

1. When do the new riskless principal trade-reporting rules go into effect?

The rules go into effect on September 30, 1999, at which time market participants will be required to report transactions according to the new rules.

2. Do the new riskless principal rules apply to Nasdaq securities, as well as all other securities traded in the over-the-counter market?

The new riskless principal rules apply to Nasdaq National Market® Securities (NNM), Nasdaq SmallCap℠ Securities (SmallCap), Over-the-Counter Bulletin Board securities (OTCBB), Nasdaq convertible debt securities, and all other securities traded in the over-the-counter market (*e.g.*, pink sheet securities). The riskless principal rules described in this *Notice to Members* do **not** apply to Third-Market transactions in exchange-listed securities. Rather, a separate rule proposal that specifically covers transactions in the Third Market was recently approved by the SEC, which is separately described in *Notice to Members 99-66.*

3. Do the new rules define what is a "riskless principal" transaction?

Existing NASD trade-reporting rules define "riskless principal" transactions effected by non-Market Makers, and require non-Market Makers that execute riskless principal transactions to not report the offsetting transaction with the non-Market Maker's customer to the tape. The new rules simply extend the existing riskless principal trade-reporting rules to cover transactions effected by Market Makers, provided that the transactions are done at the same price.

Under the new rules, a Market Maker reports a "riskless" principal transaction once if the Market Maker receives an order to buy (sell) a security, and then purchases (sells) the security as principal at the same price as the order in hand to satisfy the order to buy (sell). Generally, a riskless principal trade involves two orders, the execution of one being dependent upon the receipt or execution of the other; hence, there is no "risk" in the interdependent transactions when completed. Only when the condition or dependency is satisfied is the offsetting trade effected, the transaction completed, and only a single trade report required. Such condition may involve an institutional customer order, the execution of which is dependent upon finding the other side, in whole or in part, or a transaction dependent upon the execution of all or a part of the order placed with another firm or market. To the extent that any of the order is offset with another principal execution, that portion is deemed riskless and should be reported only once. If a portion of the order is not offset with another principal transaction, that portion would represent risk and should be reported to the tape. **See** Question 16 for an example. Additionally, as set forth in more detail in Question 4, if a member finds the other side of an institutional order and matches off the orders, the presumption will be that the trade is riskless principal.

4. How does a member determine whether transactions are at the "same price"?

In order for a transaction to be reported as riskless under the new rules, the price of the initial transaction and the offsetting transaction with the customer must be the same when the markup or markdown, commission equivalent, or other fee is excluded from the transaction prices. To determine whether two transactions are at the same price, members generally must compare the price reported to the Automated Confirmation Transaction Service℠ (ACT℠) pursuant to NASD trade-reporting rules (which require members to exclude any markup or markdown, commission equivalent, or other fee when trade reporting) and the "net price" of the offsetting trade with the customer (*i.e.*, the price to the customer, exclusive of any markup or markdown, commission equivalent, or other fee). If the tape price and the net price to the customer are the same, then the transaction must be reported as riskless principal to ACT and the offsetting leg with the customer should not be reported to ACT.

Additionally, if a Market Maker is executing a large order through a series of trades and has an arrangement to charge the customer an average price based on the various executions received, the net price to the customer and the volume weighted average price (VWAP) of the trades must be the same for the transaction to receive riskless principal treatment. **See** Question 20 for an example. To this end, when a Market Maker is attempting to fill a large order through a series of trades during the trading day, the Market Maker must be able to identify which trades were effected from inventory to fill the customer order if the Market Maker is claiming riskless principal treatment for a transaction or a portion thereof; otherwise, the Market Maker is at risk and cannot report as riskless principal. **See** Question 17 for an example.

Finally, if a member is working an order for an institutional account (as defined in NASD Rule 3110(c)(4))

or of a block size (10,000 shares or greater and at least $200,000) and the member finds the other side of the order, the presumption will be that the orders will be matched off at the same price (exclusive of any markup or markdown, commission equivalent, or other fee) and reported as riskless principal, unless the customer has specifically requested that the order be traded on a net basis at a different price.

5. Do riskless principal transactions *only* apply to retail customer orders and limit orders?

No. The rules apply to orders held by a member that are from a customer, another member, the customer of another member, or any other entity including non-member broker/dealers. Further, the rule covers both market and limit orders.

6. Do the rules prohibit "net" trading? In other words, do the rules require Market Makers to trade at one price when executing two offsetting institutional orders or when filling an institutional order out of a position the Market Maker accumulated to fill that order in hand?

The rules do not prohibit Market Makers from trading on a net basis. Nor do the rules mandate the prices at which Market Makers must execute the various legs of "riskless principal" transactions. Thus, a Market Maker is not precluded from accumulating a position at one price and executing the offsetting trade with the customer at another price (with no markup, markdown, commission equivalent, or other fee), provided that such arrangement satisfies the member's best execution obligations and is consistent with SEC and NASD statements regarding the matching of limit and market orders.[2] The rules establish, however, the requirements of how transactions should be reported if they are riskless and meet the requirements/definition of riskless principal (*i.e.*, both legs of the transaction are effected at the same price).

The NASD recognizes that there are times when a Market Maker will, while holding a customer's order, effect a buy (sell) at one price and an offsetting sell (buy) with the customer at another price, such as when a Market Maker is trading "net" with an institution. If what otherwise would appear to be a riskless principal trade is effected at two different net prices, a Market Maker would be required to report both legs of the transaction to the tape. However, if a member is working an order for an institutional account or a block size and the member finds the other side of the order, the presumption will be that the orders will be matched off at the same price (exclusive of any markup or markdown, commission equivalent, or other fee) and reported as riskless principal, unless the customer has specifically requested that the order be traded on a net basis at a different price.

The NASD believes that Market Makers should endeavor to trade at one price when executing riskless principal transactions because this will provide greater transactional integrity and will have the corollary benefit of reducing SEC transaction fees (commonly know as "Section 31 fees"). This is particularly true for customer limit orders as well as other limit orders that are not of a block size or for an institutional account.

As indicated above, the new rules do not change current trade-reporting requirements for non-Market Makers that effect riskless principal transactions.

7. Do the new rules preclude Market Makers from effecting and separately reporting riskless principal trades at different prices?

NASD rules do not prohibit Market Makers from reporting trades at two different prices of what essentially is a riskless principal trade, assuming of course the Market Maker is complying with best execution obligations. As noted above, however, if a member is working an order for an institutional account and the member finds the other side of the order, the presumption will be that the orders will be crossed at the same price (exclusive of any markup or markdown, commission equivalent, or other fee) and reported as riskless principal, unless the customer has specifically requested that the order be traded on a net basis at a different price.

8. How should I mark my ACT trade report for riskless principal trades?

Members should mark the ACT report with the capacity indicator for riskless principal (*i.e.*, click on the "Riskless" button under the P/A field on the ACT report).

9. If one leg of the transaction is executed through Nasdaq's Small Order Execution System℠ (SOES℠) or SelectNet℠ system, the system automatically reports the trade for the market participants and appends a principal capacity indicator to the trade report when a Market Maker is involved. When this occurs and the trade is part of a riskless principal transaction, is the Market Maker required to go back into ACT and change the system-generated trade report to indicate the trade was riskless principal?

Generally, no. If a trade is executed through SOES or SelectNet, the trade is automatically reported to ACT and sent to the tape. When a trade involves a Market Maker, ACT defaults to a capacity indicator of "principal" on the trade report. For SOES and SelectNet trades, a Market Maker will **not** be required to go back into ACT and change the Nasdaq system-generated ACT report to indicate the trade was effected on a riskless principal basis. If, however, the Market Maker does not clear for the customer for which it executed the riskless principal trade, the Market Maker will be required to submit a "clearing-only" record to ACT and to the NSCC. In these instances, the Market Maker is required to indicate on the "clearing only" record that the trade was done on a riskless principal basis.

For example, MMA receives a customer limit order to buy at $20 from another member, and displays that order in its quote. SOES executes against MMA's quote thus taking out the $20 buy order, and SOES reports the trade to the tape at $20 as principal for MMA. If MMA does not clear for the member from which it received the customer limit order, MMA would be required to enter a clearing-only record into ACT to reflect the offsetting sale to the member at $20, and would be required to indicate on the clearing record that the trade was done on a riskless principal basis.

For riskless principal transactions that occur outside Nasdaq systems (*e.g.*, phone orders or internal executions) the Market Maker must report the initial leg to ACT and mark the ACT report as riskless principal. Additionally, depending on whether the Market Maker clears for the customer, the Market Maker may also have to submit a "clearing only" record to ACT, which also must indicate the trade was done as riskless principal.

10. If a Market Maker does not report a trade with a customer to ACT because the trade qualifies for riskless principal treatment, is the Market Maker still required to input that information into the Order Audit Trail System (OATS℠)?

Yes. If Market Maker A (MMA), for example, represents in its quote a limit order to buy 100 shares at $20, and Market Maker B (MMB) hits MMA's bid, MMA will not be required to report to ACT the offsetting sale of 100 shares at $20 to the customer. MMA will, however, be required to report this information to OATS. Specifically, MMA should report the receipt of the order via a "New Order Report" and the execution of the customer order via an "OATS Execution Report." On the OATS Execution Report, MMA should supply a Reporting Exception Code of "M" (M = Market Maker side of Nasdaq execution system execution). The Reporting Exception Code indicates that there is no corresponding trade report in ACT.

11. Aren't Market Makers always at risk? For example, if a Market Maker is holding an order and is accumulating a position in an attempt to fill the order, isn't the Market Maker at risk because the customer may cancel the order before the Market Maker finds the other side and fills it? How will a firm know if a trade is riskless?

Market Makers are not necessarily **always** at risk for purposes of trade reporting. A Market Maker generally is not at risk if the Market Maker has two orders in hand that it is crossing at the same price or if the Market Maker has one order for which execution is contingent upon finding the other side at the same price.

As a rule of thumb, a Market Maker's responsibility to report to ACT the second leg of the transaction with the customer is determined after the Market Maker has accumulated a position and/or found the other side, and the Market Maker wishes to effect an offsetting transaction with the customer. Generally, if after accumulating a position to fill a customer order, the Market Maker actually fills such order, the Market Maker is not at risk on the second leg of the transaction and will not report the customer fill to ACT. Conversely, if the customer cancels the order while the Market Maker is accumulating a position, the Market Maker becomes "at risk" for the amount it has accumulated and is holding in inventory. Accordingly, when the Market Maker attempts to liquidate that position, the Market Maker must report the associated trade(s) to the tape.

12. If a customer cancels an order while a Market Maker is in the process of accumulating a position to fill the customer's order, the ACT report will show a riskless principal modifier when these trades are really "at risk." Will this be a violation of NASD rules?

There may be times when a Market Maker has accumulated a portion or all of a position to satisfy a customer order in hand, has reported those transactions to the tape as riskless principal, and the customer cancels the order prior to the Market Maker filling it. The member will not be in violation of riskless principal rules provided that the member properly documents that the trade(s) was reported to ACT as riskless principal while the member was holding a customer order and that the customer canceled the order. The member should keep accurate records reflecting the time the customer order was received and canceled, as well as the execution time(s) of the trade(s) reported as riskless principal.

13. Are the new rules for riskless principal trade reporting mandatory?

Yes. If a transaction meets the definition of "riskless principal" in the new trade-reporting rules (*i.e.*, two orders that offset one another that are executed at the same price), market participants must report once and as riskless principal.

Trade-Reporting Requirements

14. Nasdaq Inside Market: $20 - 20 1/4, 10 X 20

MMA is at the inside offer displaying its customer's limit order to sell 2,000 shares at $20 1/4 when MMB lifts the offer using the phone. What are MMA's trade-reporting obligations?

MMA should report to ACT the sale of 2,000 shares to MMB and mark the report with a riskless principal capacity indicator. Since MMA then buys from the customer at a price of $20 1/4, MMA will not report to ACT the offsetting buy at $20 1/4 from the customer.

15. If I am a Market Maker in a Nasdaq-listed security and I am engaging in a riskless principal trade consistent with the new trade-reporting rule, how do I confirm the transaction to my customer under SEC Rule 10b-10? For example, what would I have to confirm in the transaction described in Question 14?

SEC Rule 10b-10(a)(2)(ii)(B) requires a Nasdaq Market Maker that trades as principal to disclose on the confirmation:

1) the "reported trade price" for the trade between the Market Maker and the customer (net price or reported trade price);

2) the price to the customer (gross price); and

3) the difference (if any) between the reported trade price and the price to the customer (*e.g.*, markup, markdown, commission equivalent, or other fee).

Under the riskless principal trade-reporting rules, if a Market Maker executes a riskless principal transaction where the tape price and the net price to the customer are the same, the Market Maker would not report the offsetting transaction with the customer to the tape. Thus, there technically would be no "reported trade price" (Item #1 above) for the purpose of Rule 10b-10 confirmation requirements, since the transaction with the customer would not be reported to the tape. After consultation with the SEC, it appears warranted that in these instances, the Market Maker would disclose on the confirmation:

A) the price that was reported to the tape for the first leg of the transaction, as the "reported trade price" (Item #1, above);

B) the price to the customer (*i.e.*, the gross price of the buy/sale to the customer); and

C) the difference (if any) between the reported trade price and the gross price to the customer (*i.e.*, Item A and Item B).

With regard to Question 14, assume that MMA, which was reflecting a limit order to sell at 20 1/4, tacked on no markdown or other fee. In that case, MMA would confirm to the customer:

A) a trade price of $20 1/4 (the first leg of the transaction that was reported to ACT by MMA);

B) a price to the customer of $20 1/4; and

C) a no differential.

If MMA had added a commission equivalent of 1/4, MMA would have confirmed:

A) a trade price of $20 1/4;

B) a price to the customer of $20; and

C) a differential of 1/4.

Members should note that while the disclosure requirements of SEC Rule 10b-10(a)(2)(ii)(B) do not apply to Market Makers in non-Nasdaq OTC securities (pink sheet and OTCBB securities), the NASD currently is considering adopting a parallel disclosure requirement for non-Nasdaq OTC Market Makers.

Finally, for riskless principal trades effected by non-Market Makers trading as principal in Nasdaq and OTC securities, SEC Rule 10b-10 confirmation requirements remain the same as they are today.[3]

16. Nasdaq Inside Market: $10 - 10 1/4, 10 X 10

MMA receives from an institutional customer an order to sell 100,000 shares with instructions to work the order with a price limit (or "bottom") of $10 1/8. The customer tells MMA that it is willing to pay a markdown, commission equivalent, or other fee of 1/8 below the $10 1/8 price. Using the phone, MMA sells 75,000 shares to MMB at a price of $10 1/8 per share. Instead of attempting to find the remaining 25,000 shares, MMA fills the entire customer order for 100,000 shares, for a price of $10 1/8 per share (exclusive of any markdown, commission equivalent, or other fee), by

trading the 25,000-share balance out of inventory. How is this trade reported? Is part of the order deemed to be "at risk" and part of the order considered to be riskless?

Only a portion of the 100,000-share transaction is deemed to be riskless – the 75,000 shares. The remaining 25,000 shares that were executed from MMA's inventory are considered to be "at risk," and must be reported to the tape. Thus, MMA will report the sale to MMB of 75,000 shares at $10 1/8 in one ACT report, and separately report the offsetting buy of 25,000 at $10 1/8 from its institutional customer. MMA reports only a buy of 25,000 and not a buy of 100,000 shares from its institutional customer because the 25,000 is deemed to be "at risk." The confirmation to the customer would show a reported price of $10 1/8, a price to the customer of $10, and a differential (markdown) of 1/8.

17. In the above example, it may not be easy for MMA to definitively say that 75,000 shares were riskless, because MMA may have accumulated these shares in multiple transactions throughout the entire day. Can MMA still report these as riskless principal?

No. In order for a Market Maker to report trades as riskless principal, the Market Maker must be able to identify a specific trade or a group of trades (which may be effected at one price level or multiple price levels if the customer is receiving a VWAP) as being those utilized to fill a customer order. If a member cannot identify which trade or series of trades were effected to offset a customer order, the Market Maker is at risk and cannot report as riskless principal.

Thus, in the question above where MMA was claiming 75,000 shares were riskless principal, MMA must be able to tie a specific trade or trades to the 75,000. If MMA were reporting an average price of $10, MMA would have to point to a series of transactions which had an average price of $10 (exclusive of markups or markdowns, commission equivalents, or other fees) and which totaled 75,000 shares.

18. Nasdaq Inside Market: $10 - 10 1/4, 10 X 10

MMA is at the inside bid displaying a customer limit order to buy 1,000 shares at $10, when MMA receives a market order to sell 500 shares over SOES, which is automatically executed against MMA's quote and reported to the tape. What are MMA's trade-reporting obligations?

Under NASD Rule 2110 and IM-2110-2 (commonly know as "Manning"), MMA is obligated to execute at least 500 shares of the limit order it is holding. Thus, MMA can sell 500 shares on a riskless principal basis to the customer at $10, not report the transactions to the tape, and display the remaining 500 shares in its quote. Alternatively, MMA can sell 1,000 shares to the customer limit order at $10, and report 500 shares to the tape as the 500 are deemed to be at risk.

19. Nasdaq Inside Market: $25 - 25 1/8, 10 X 10

MMA receives a not-held order from an institutional customer to buy 5,000 shares, with instructions to work the order with a price limit (or "top") of $25 1/16. MMA's customer tells it that he wishes to trade net and does not wish to pay a markup, markdown, commission equivalent, or other fee over and above the $25 1/16 top price. Using SelectNet, MMA buys 5,000 shares from MMB at $25, and SelectNet reports the transaction to the tape. What are MMA's reporting obligations?

Assuming that MMA sells the 5,000 shares to its customer at $25 1/16 net, MMA must report this sale to the tape because the reported price via SelectNet and the offsetting sell to its customer were done at different prices.

If MMA were not trading net and, for example, sold to its customer at $25, plus a 1/16 mark-up or sales credit, MMA would not report the sale to the customer to ACT since the two trades were done at the same price. Under SEC Rule 10b-10, the confirmation to the customer would show a reported price of $25, a price to the customer of $25 1/16, and a differential of 1/16. This answer is consistent with statements made by the NASD in *Notices to Members 95-67* and *96-10*, as well as the letter from Richard Lindsey, SEC, to Richard Ketchum, NASD, dated January 3, 1997.

20. Nasdaq Inside Market: $10 - 10 3/8, 10 X 10

MMA receives a not-held order from an institutional customer to sell 6,000 shares, with instructions to obtain the best price available with a "bottom" of $10 1/8. Using the phone, MMA sells 4,000 shares at $10 3/8 to MMB and 2,000 shares at $10 to MMC. What are MMA's trade-reporting obligations?

MMA must report to ACT the sell to MMB of 4,000 shares at $10 3/8 and the sell to MMC of 2,000 shares at $10. (Note that the VWAP for this trade is $10 1/4). If MMA buys 6,000 shares from its customer at a VWAP of $10 1/4, it will not be required to report to the tape the offsetting buy with the

customer. The NASD believes that it would be consistent with an SEC No-Action Letter regarding SEC Rule 10b-10 for MMA to disclose on the confirmation a reported price of $10 1/4 — the VWAP — instead of a reported price for each individual transaction.[4] The confirmation must contain a notation that the disclosed price is an average price, and must note that details regarding the actual prices are available to the customer upon request.[5] If MMA charged a markdown, commission equivalent, or other fee on top of the $10 1/4, it also would be permissible for the confirmation to disclose the fee as a single amount.

Alternatively, if MMA trades on a net basis and buys 6,000 shares from its customer at $10 1/8 (or any other price different from the VWAP of $10 1/4), MMA would report the buy with its customer to the tape because VWAP and the buy from the customer were different prices. The confirmation would disclose a reported price of $10 1/8, a price to the customer of $10 1/8, and no differential.

21. Nasdaq Inside Market: $10 - 10 1/4, 10 X 10

MMA receives an order to buy 10,000 shares at a limit price of $10 1/8 from Institutional Customer 1, and simultaneously receives an order to sell 10,000 shares at a limit price of $10 1/8 from Institutional Customer 2. MMA buys 10,000 shares from Institutional Customer 2 and sells 10,000 to Institutional Customer 1, both at $10 1/8. How is this reported?

MMA reports the sale to Institutional Customer 1 as riskless principal of 10,000 shares at $10 1/8, assuming that the trades were effected from MMA's market-making account. There will be no trade report for the buy from Institutional Customer 2. MMA will confirm the respective transactions to both customers consistent with SEC Rule 10b-10.

If the transaction had been effected as a pure agency cross and the trades were not run through MMA's market-making or proprietary account, MMA would report the transaction as an agency cross, not as riskless principal.

22. Nasdaq Inside Market: $10 - 10 1/4, 10 X 10

MMA receives an order to buy 100,000 shares at a limit price of $10 1/8 from Institutional Customer 1, and simultaneously receives an order to sell 75,000 shares at a limit price of $10 1/8 from Institutional Customer 2. MMA crosses 75,000 shares and in order to fill the remainder of Institutional Customer 1, sells 25,000 shares at $10 1/8 to the customer. How is this trade reported?

One ACT report would indicate an agency cross of 75,000 since the trade was effected as agent and not through MMA's market-making account. MMA would submit a separate trade report that would indicate a sale of 25,000 shares at $10 1/8 as principal. Note that the confirmation to Institutional Customer 1 would indicate that the firm acted both as principal and agent, consistent with the SEC No-Action Letter.[6]

Attachment B – Text Of Rule Changes

(Note: New text is underlined; deletions are in brackets.)

4630. Reporting Transactions in Nasdaq National Market Securities

4632. Transaction Reporting

(a) through (c) No Change

(d) Procedures for Reporting Price and Volume

(1) through (3)(A) No Change

(B) Exception: A "riskless" principal transaction in which a member [that is not a market maker in the security] after having received [from a customer] an order to buy a security, purchases the security as principal [from another member or customer] at the same price to satisfy the order to buy or, after having received [from a customer] an order to sell, sells the security as principal [to another member or customer] at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee.

(e) through (f) No Change

4640. Reporting Transactions in Nasdaq SmallCap Market Securities

4642. Transaction Reporting

(a) through (c) No Change

(d) Procedures for Reporting Price and Volume

(1) through (3)(A) No Change

(B) Exception: A "riskless" principal transaction in which a member [that is not a market maker in the security] after having received [from a customer] an order to buy a security, purchases the security as principal [from another member or customer] at the same price to satisfy the order to buy or, after having received [from a customer] an order to sell, sells the security as principal [to another member or customer] at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee.

(e) through (f) No Change

4650. Reporting Transactions in Nasdaq Convertible Debt Securities

4652. Transaction Reporting

(a) through (c) No Change

(d) Procedures for Reporting Price and Volume

(1) through (3)(A) No Change

(B) Exception: A "riskless" principal transaction in which a member [that is not a market maker in the security] after having received [from a customer] an order to buy a security, purchases the bond as principal [from another member or customer] at the same price to satisfy the order to buy or, after having received [from a customer] an order to sell, sells the bond as principal [to another member or customer] at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee.

(e) through (f) No Change

6600. Reporting Transactions In Over-The-Counter Equity Securities

6620. Transaction Reporting

(a) through (c) No Change

(d) Procedures for Reporting Price and Volume

(1) through (3)(A) No Change

(B) Exception: A "riskless" principal transaction in which a member [that is not a market maker in the security] after having received [from a customer] an order to buy a security, purchases the security as principal [from another member or customer] at the same price to satisfy the order to buy or, after having received [from a customer] an order to sell, sells the security as principal [to another member or customer] at the same price to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the mark-up or mark-down, commission-equivalent, or other fee.

(e) No Change

Endnotes

[1]In fact, NASD Rule IM-2110-2 (Limit Order Protection Rule) requires Market Makers to execute customer limit orders (regardless of whether the customer is theirs or that of another member) when trading as principal at prices that would satisfy the customer's limit order. In addition, pursuant to best execution obligations articulated by the SEC under the SEC Order Handling Rules, Market Makers generally must pass along any price improvement obtained when executing an incoming order at its published quote while holding an undisplayed limit order priced better than that quote. *See Notice to Members 97-57*.

[2]*See* Exchange Act. Release No. 34-37619A (Sept. 6, 1996), 61 FR 48290 (Sept. 12, 1996) (Order Handling Rules Adopting Release); NASD *Notice to Members 96-65* (October 1996); NASD *Notice to Members 97-57* (September 1997).

[3]*See* SEC Rule 10b-10(a)(2)(ii)(A).

[4]*See e.g.,* SEC No-Action Letter from Catherine McGuire, SEC, to Eugene Lopez, The Nasdaq Stock Market, dated May 6, 1997 (permitting the issuance of a single confirmation at an average price and with multiple capacities for a single customer order effected with multiple executions).

[5]*See id*.

[6]*See id*.

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NASD Notice to Members 99-66

SEC Approves Prior Reference Price Trade Modifier, Changes To Bunching Rules, And Riskless Principal Trade-Reporting Rules For The Third Market

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Executive Summary

On July 8, 1999, the Securities and Exchange Commission (SEC or Commission) approved a rule change to:

1) implement a new trade report modifier to identify trades effected at a prior reference price (.PRP modifier);

2) eliminate the 10,000-share limitation on individual trades that may be "bunched" for trade-reporting purposes for trades that are effected on the first day of secondary market trading; and

3) require Market Makers in the Third Market to report trades under the current riskless principal rules that apply to non-Market Makers in the Third Market.

Additionally, on July 23, 1999, the SEC approved a rule change to eliminate an unnecessary provision in National Association of Securities Dealers, Inc. (NASD®) Rule 6420 relating to the reporting of transactions in exchange-listed securities traded in the Third Market.

This *Notice* includes questions and answers regarding the rule changes (Attachment A); and the text of the rule changes (Attachment B). The rule changes go into effect on September 30, 1999.

Questions/Further Information

Questions concerning this *Notice* may be directed to the Office of General Counsel, The Nasdaq Stock Market, Inc., at (202) 728-8294 or the Legal Section, Market Regulation, NASD Regulation, Inc., (NASD Regulation®) at (301) 590-6410.

Discussion

1. Prior Reference Price Modifier

Nasdaq® is implementing a new modifier to report late executions (as distinguished from late trade reports), which will be used for trade reports in Nasdaq securities (both Nasdaq National Market® (NNM) and SmallCap℠ securities) and non-Nasdaq over-the-counter equity securities (*e.g.*, OTC Bulletin Board® and pink sheets).

Recently there have been situations in which members execute certain transactions that, although reported timely, actually relate to an obligation to trade that arose at an earlier point in the day or that refer to a prior reference price. These situations include:

1) obligations to trade arising from a preferenced SelectNet℠ order that was not executed timely;

2) orders that are owed the opening or closing price ("market on open" and "market on close") but that are not executed within 90 seconds of the open or close of the market, respectively; and

3) orders that may have been lost or misplaced and later filled.

In effect, these trades are late executions, not late reports of executions.

To enable market participants to more accurately report late executions (which many firms today report as .SLD trades), Nasdaq is implementing a new trade report modifier, called the ".PRP" modifier. This modifier must be appended to trade reports that reflect a price that is different from the current market because the execution is based on

a prior reference point in time. Additionally, when using the .PRP modifier, members are required to input the prior reference time (*i.e.*, the time the obligation to trade arose), which shall be placed in the execution time field on the Automated Confirmation Transaction Service℠ (ACT℠) report.

The following principles and requirements apply to members when using the .PRP modifier:

- Members must use the .PRP modifier for trade reports in Nasdaq securities (both NNM and SmallCap securities), and non-Nasdaq over-the-counter equity securities (*e.g.*, OTC Bulletin Board and pink sheets). Members may not use the .PRP modifier for trades in exchange-listed stocks that are effected in the Third Market.

- Members may not use the .PRP modifier in "stop" stock situations.

- The .PRP modifier will not be required to be used if the report is made within 90 seconds of the prior reference time.

- It will no longer be appropriate for firms to use the .SLD modifier to report late executions; the .SLD modifier may only be used to report late reports of execution.

- Use of the .PRP modifier does not absolve the member of its obligation to provide best execution, in terms of both price and timely execution.

The following are some specific examples of when the .PRP modifier would be used:

Example 1. A member receives a preferenced SelectNet order at the member's quote ("liability order") at 11:00 a.m. The member fails to execute the trade. Thirty minutes later, at 11:30 a.m., this is brought to the attention of the receiving member, which agrees that the trade should have taken place at 11:00 and at the price existing at 11:00. The receiving member then executes a trade at the 11:00 price. Under the rule change, the member must append a .PRP to the trade report and must input the time "11:00."

Example 2. A member receives a large number of customer orders prior to the open, which are to be executed at the opening print. Once that price can be identified, the member's system begins executing each trade at that price. Any such trade that is executed at the opening but due to heavy volume is not printed until after 9:31:30 should be identified with the .SLD identifier. If, however, at 9:45 the member discovers that a customer's order that should have been executed at the open has not yet been executed, it would be appropriate to execute that customer's order and append the .PRP modifier with the time "9:30." This tells market participants that the execution price represents a price that relates to an earlier point in time (in this case, the open), and thus may not bear any relation to the current market, which may have moved in the interim.

2. Partial Elimination of the 10,000 Share Limitation on Bunching of Trades

NASD trade-reporting rules for NNM and SmallCap securities currently permit members to aggregate transactions into a "bunched" trade report in a variety of situations. In particular, the rules permit a member to aggregate transactions done at the same price when it would be impractical to report the trades individually. The rule provides, however, that when reporting bunched trades no individual order of 10,000 shares or more may be aggregated and reported. The rule further provides that bunched trades must be reported within 90 seconds of the initial transaction and the report must include a ".B" modifier.

Under the rule change approved by the SEC, Nasdaq is removing the 10,000-share limitation for bunching *but only for trades effected on the first day of secondary market trading following an initial public offering (IPO).* The 10,000-share cap will continue to apply for trades effected after the first day of secondary market trading of an IPO (*i.e.,* day two onward of secondary-market trading). The lifting of the cap for first-day secondary market trading will facilitate more efficient and timely reporting of large numbers of trades in the immediate aftermarket. As is the case today, bunching is optional and a member may continue to report trades individually.

3. Trade-Reporting Rules for Riskless Principal Trades in the Third Market

Under current trade-reporting rules for the Third Market, non-Market Makers generally do not report the offsetting trade with a customer when a "riskless principal" transaction is involved (*i.e.*, a transaction that involves a trade with another member, usually a Market Maker, which is used to offset a trade with a customer). This "riskless principal exception" results in one trade report even though the non-Market Maker firm is involved in two separate trades against its principal account.

Due to recent growth and changes in Third Market trading, including significant advances in technology and the implementation of the SEC's order handling rules, Nasdaq

sees no significant reason to continue the distinction between Market Makers and non-Market Makers in the context of the Third Market, and thus is extending this riskless principal exception described above to Market Makers in the Third Market. Under the rule change, only one trade report will result for transactions where the Market Maker has encountered no risk and, although there are two trades effected, the economic reality is that the trades can be viewed as one trade. For example, if a Market Maker in an exchange-listed security does not assume a risk position on an Intermarket Trading System (ITS) commitment sent to another market center, the Market Maker will not reprint the trade in the Third Market when it receives confirmation of an execution on the commitment. This analysis applies to transactions that result from orders sent to the floor even when sent outside of the ITS linkage (*e.g.*, through a floor broker or other automated execution system of the exchange) as well as other Market Makers in the Third Market.

The rule defines "riskless principal" as a trade in which a member, after having received an order to buy (sell), purchases (sells) the security as a principal in order to satisfy the order to buy (sell). Thus, a riskless principal trade generally is one that involves a conditional order rather than one immediately executable by the firm as principal. Such condition may involve a customer order for which execution is dependent upon finding the other side, or a transaction dependent upon the execution of a part of the order placed with another firm or market. For example, after receiving a customer's market order to buy 500 shares, a Market Maker in the Third Market sends an order to an exchange for 1,000 shares, where it is immediately executed. The Market Maker then satisfies the 500-share order for its customer. The 1,000-share execution is reported by the exchange; under the new rules, the 500-share execution by the Market Maker will not be printed again in the Third Market. The remaining 500 shares that the Market Maker bought on the floor of the exchange, however, is deemed to be "at risk." Accordingly, if the Market Maker sells those 500 shares in a later transaction, the Market Maker will print the 500 shares in the Third Market.

Under the rule, there may be situations where only a portion of a transaction may be riskless and reported as such. That is, to the extent that the customer's order is greater than the first leg that is executed on an exchange or in the Third Market, only the portion of the second leg *(i.e.,* the offsetting transaction with the customer) that is offset by the first leg will be deemed riskless; any balance would be "at risk" and reported as a separate trade. Thus, if a portion of a larger transaction is being filled from a Market Maker's inventory, that portion of the trade filled from inventory must be reported as principal. For example, after having received an order to buy 1,000 shares, a Market Maker in the Third Market fills 500 shares from inventory and sends an order for 500 shares to an exchange. The exchange reports back to the Market Maker an execution of 500 shares. The Market Maker then fills the 1,000-share customer order. The Market Maker would only report 500 shares in the Third Market (the amount filled from inventory) and would not report the 500-share execution received on the floor of the exchange because that portion of the trade is deemed riskless.

Marker Order Exception. Nasdaq also considered the extent to which the riskless principal definition would apply in situations where the first leg is a "marker" order. These orders, usually of nominal size, are used to trigger obligations to other orders the firm may be holding. Marker orders serve as a mechanism to notify the Market Maker that the market has traded at that price and that a conditional order the Market Maker is holding has now become executable in accord with the firm's understanding with its customer. Marker orders generally are not intended to offset, to any significant degree, other executions by the Market Maker.

Nasdaq has determined to add an exception to the riskless principal trade-reporting rule for marker orders that are 10 percent or less than the full size of the order or group of orders being marked. That is, the execution of a marker order would appear to merit riskless principal treatment and would not be printed in the Third Market to the extent of the size of the marker order. However, given the purpose for which marker orders are used, a member should not be required to break up the order it is holding into two separate components to distinguish between a risk and riskless portion, if the marker order is no larger than 10 percent of the size of an execution or group of executions that it would trigger. This is because the nominal size of the marker order does not, to any material extent, change the overall risk profile of the order. (**See** Questions 16 and 17 in Attachment A for examples on handling marker orders.)

10b-10 Obligations. In the order approving the Third Market riskless principal rules, the SEC stated that Rule 10b-10 under the Act requires a broker/dealer acting as Market Maker in a riskless principal transaction in an exchange-listed security to confirm to its customer:

1) the reported trade price;

2) the price to the customer in the transaction; and

3) the difference, if any, between the reported trade price and the price to the customer (*i.e.,* any markup or markdown, commission equivalent, or other fee on top of the reported price).

The SEC further stated that under Rule 10b-10, the broker/dealer is required to report, as the "reported trade price", the price at which the security was reported to the tape (Consolidated Tape Authority (CTA)) by the exchange or Market Maker in the Third Market when the member purchased the security for, or sold the security on behalf of, its customer. The Commission stated that this requirement remains in effect regardless of the fact that there is no corresponding requirement in the NASD rules to report the second leg of a riskless principal transaction to the tape.

4. Elimination of "Reasonably Related to the Market" Provision in NASD Rule 6420

In addition to the changes to Third Market trade-reporting rules described above, the SEC approved on July 23, 1999, a rule change that eliminates unnecessary provisions of NASD Rule 6420.

NASD Rule 6420(d)(3)(A), which is the general rule requiring NASD members to report all principal transactions in exchange-listed securities in the Third Market, contains language requiring members to report transactions in a manner "reasonably related to the prevailing market taking into consideration all relevant circumstances..." (Reasonably Related to the Market Provision). The Reasonably Related to the Market Provision was added as part of broader changes in 1980 to the Third Market trade-reporting rules, which at the time required Market Makers in the Third Market to report to the tape transaction prices inclusive of any markup, markdown, commission equivalent, or other fee to the customer (collectively, charges).[1] In contrast, exchange rules at the time required their members to report to the tape transaction prices exclusive of any charges to the customer. The 1980 changes to the Third Market trade-reporting rules were intended to make comparable the reporting of Third Market trades with exchange transactions by requiring Market Makers in the Third Market to report trades exclusive of any charges.

Since the 1980 rule changes, Nasdaq has come to the conclusion that the Reasonably Related to the Market Provision is superfluous in the context of Third Market trading and does not serve any meaningful purpose with respect to the trade reporting for these securities. Indeed, this provision has served only to promote the misinterpretation that the rule provides flexibility in the manner in which NASD members may report Third Market transactions, which has led some to believe there is inaccurate trade reporting in the Third Market. To be certain, NASD rules do not permit such discretion or latitude — Market Makers in the Third Market must report to the tape transaction prices **exclusive** of any charges. Additionally, under Exchange Act Rule 10b-10 Market Makers in the Third Market must confirm to the customer the price reported to the tape and any difference between the price reported to the tape and the price to the customer.

Additionally, as the SEC recently stated in the context of a proposal to extend the NASD's ITS/CAES linkage to all exchange-listed securities, while the Commission appears to concur that the rules could be clarified, the rules are nonetheless the same for the reporting of both 19c-3 securities and non-19c-3 securities. Nasdaq believes that NASD rules and procedures, along with a member's best execution obligations, provide the necessary protections to ensure accurate and appropriate trade reporting in exchange-listed securities. As the Commission has indicated on several occasions, an effective surveillance program along with the requirements of Exchange Act Rule 10b-10, ensure compliance with trade-reporting obligations and the proper disclosure of any markup or markdown.[2] Accordingly, Nasdaq is removing this less-than-clear language from the rule to ensure there are no continuing ambiguities or misinterpretations.

Attachment A — Questions And Answers

General Questions

1. When do the new riskless principal rules for the Third Market go into effect?

The rules go into effect on September 30, 1999, at which time NASD members which effect transactions in the Third Market will be required to report transactions according to the new rules.

2. Do the riskless principal rules described in this *Notice* apply only to transactions in exchange-listed securities effected in the Third Market?

Yes. The new riskless principal rules apply only to transactions in exchange-listed securities effected in the Third Market by NASD members. The rules described in this *Notice* are separate and different from the riskless principal rules that were recently adopted for Nasdaq and over-the-counter securities, which are described in more detail in NASD *Notice to Members 99-65.*

3. Do the new rules define what is a "riskless principal" transaction?

Existing NASD trade-reporting rules for the Third Market define "riskless principal" transactions effected by non-Market Makers, and require non-Market Makers that execute riskless principal transactions to not report the offsetting transaction with the non-Market Maker's customer to the NASD. The new rules simply extend the existing riskless principal trade-reporting rules to cover transactions effected in the Third Market by Market Makers.

Under the new rules, a Market Maker reports a "riskless" principal transaction once if the Market Maker receives an order to buy (sell) a security, and then purchases (sells) the security as principal to satisfy the order to buy (sell). Generally, a riskless principal trade involves two orders, the execution of one being dependent upon the receipt or execution of the other; hence, there is no "risk" in the interdependent transactions when completed. Only when the condition or dependency is satisfied is the offsetting trade effected, the transaction completed, and only a single trade report required. Such condition may involve an institutional customer order, the execution of which is dependent upon finding the other side, in whole or in part, or a transaction dependent upon the execution of all or a part of the order placed with another firm or market. To the extent that any of the order is offset with another principal execution, that portion is deemed riskless and should be reported only once**.** If a portion of the order is not offset with another principal transaction, that portion would represent risk and should be reported to the tape to the extent it is riskless. (As noted in Question 4, there is an exception to the general rule for marker orders.) **See** Question 14 below for an example.

Thus, for example, if a Market Maker receives a customer market or marketable limit order and the Market Maker sends the order to the floor of an exchange for execution, the exchange will print the trade. When the specialist reports the trade back to the Market Maker and the Market Maker subsequently effects the offsetting transaction with its customer, the Market Maker will not report the offsetting transaction to the tape.

Finally, the NASD wishes to clarify that orders received from other broker/dealers and non-customers qualify for riskless principal treatment, although the rule only specifically refers to "customer" orders.

4. Do "marker" orders that are sent to an exchange as part of a larger order qualify for riskless principal treatment?

If a marker order is 10 percent or less than the full size of the order or group of orders it is marking, then the marker order is not considered "riskless" and would be reported as part of the larger order(s) when the offsetting trade is effected in the Third Market. For an example, see Questions 16 and 17.

5. Do riskless principal transactions *only* apply to retail customer orders and limit orders?

No. The rules apply to orders held by a member that are from a customer, another member, the customer of another member, or any other entity including non-member broker/dealers. Further, the rule covers both market and limit orders.

6. How should a member mark a trade report for riskless principal trades?

Members should mark the trade report with the capacity indicator for riskless principal (*i.e.*, click on the "Riskless" button under the P/A field on the ACT report).

7. If one leg of the transaction is executed through Nasdaq's Computer Assisted Execution System℠ (CAES℠), the system automatically reports the trade for the market participants and appends a principal capacity indicator to the trade report when a Market Maker is involved. When this occurs and the trade is part of a riskless principal transaction, is the Market Maker required to go back into ACT and change the system-generated trade report to indicate the trade was riskless principal?

Generally, no. If a trade is executed through CAES where the trade is automatically reported to ACT and sent to the tape, ACT will default to a capacity indicator of "principal" when a Market Maker is involved. When this occurs, a Market Maker will **not** be required to go back into ACT and change the Nasdaq system-generated report to indicate the trade was effected on a riskless principal basis. If, however, the Market Maker does not clear for the customer for which it executed the riskless principal trade, the Market Maker will be required to submit a "clearing-only" record to ACT and to the National Securities Clearing Corporation (NSCC). In these instances, the Market Maker is required to indicate on the "clearing-only" record that the trade was done on a riskless principal basis.

For example, Market Maker A (MMA) receives a customer limit order to buy at $20, and displays that order in its quote. Another Market Maker or market center sends an order through CAES, which executes against MMA's quote and takes out the $20 buy order. CAES then reports the trade to the tape at $20 as principal for MMA. If MMA does not clear for the customer from which it received the customer limit order, MMA will be required to enter a "clearing-only" record into ACT to reflect the offsetting sale to the customer at $20, and will be required to indicate on the clearing record that the trade was done on a riskless principal basis.

For riskless principal transactions that occur over the phone in the Third Market or via a Market Maker's internal execution system, the Market Maker must report the initial leg to the tape and mark the trade report as riskless principal. Additionally, depending on whether the Market Maker clears for the customer, the Market Maker may also have to submit a "clearing-only" record to ACT, which also must indicate the trade was done as riskless principal. Since trades which are executed on the floor of an exchange are reported by such exchange, NASD Market Makers need not report the trade to the tape or otherwise indicate the trade was done on a riskless principal basis.

8. Aren't Market Makers always at risk? For example, if a Market Maker is holding an order and is accumulating a position in an attempt to fill the order, isn't the Market Maker at risk because the customer may cancel the order before the Market Maker finds the other side and fills it? How will a firm know if a trade is riskless?

Market Makers are not necessarily **always** at risk for purposes of trade reporting. A Market Maker generally is not at risk if the Market Maker has two orders in hand that it is crossing or if the Market Maker has one order whose execution is contingent upon finding the other side at the same price.

As a rule of thumb, a Market Maker's responsibility to report to the tape the second leg of the transaction with the customer is determined after the Market Maker has accumulated a position and/or found the other side, and the Market Maker wishes to effect an offsetting transaction with the customer. Generally, if after accumulating a position to fill a customer order the Market Maker actually fills such order, the Market Maker is not at risk on the second leg of the transaction and will not report the customer fill to the tape. Conversely, if the customer cancels the order while the Market Maker is accumulating a position, the Market Maker becomes "at risk" for the amount it has accumulated and is holding in inventory. Accordingly, when the Market Maker attempts to liquidate that position, the Market Maker must report the associated trade(s) to the tape.

9. If a customer cancels an order while a Market Maker is in the process of accumulating a position to fill the customer's order, the trade report will show a riskless principal modifier when these trades are really "at risk." Will this be a violation of NASD rules?

There may be times when a Market Maker has accumulated a portion or all of a position to satisfy a customer order in hand and reported those transactions to the tape as riskless principal, but the customer cancels the order prior to the Market Maker filling it. The member will not be in violation of riskless principal rules provided that the member properly documents that the trade(s) was reported to the tape as riskless principal while the member was holding a customer order and that the customer canceled the order. The member should keep accurate records reflecting the time the customer order was received and subsequently canceled, as well as the execution time(s) of the trade(s) reported as riskless principal.

10. Are the new rules for riskless principal trade reporting mandatory?

Yes. If a transaction meets the definition of "riskless principal" in the new trade-reporting rules, market participants must report once and as riskless principal.

Trade-Reporting Requirements

11. CQS Inside Market: $20 - 20 1/4, 10 X 20

MMA, which is a Market Maker in the Third Market, is at the inside offer displaying its customer's limit order to sell 2,000 shares at

$20 1/4 when Market Maker B (MMB—another Market Maker in the Third Market) lifts the offer using the phone. What are MMA's trade-reporting obligations?

MMA must report to the tape the sale of 2,000 shares to MMB and mark the report with a riskless principal capacity indicator. MMA will not report to the tape the offsetting buy at $20 1/4 from the customer.

12. CQS Inside Market: $20 - 20 1/4, 10 X 20

MMA receives a 500-share market order to buy and sends the order to the floor of an exchange via the ITS linkage or other means (*e.g.*, through a floor broker or other automated routing or execution system of the exchange). The specialist on the exchange floor executes the trade at $20 1/4, and reports that price back to MMA. What are MMA's trade-reporting obligations?

MMA should not report the offsetting trade with its customer to the tape, since this is a riskless principal transaction and the exchange has already reported the trade to the tape.

13. If I am a Market Maker in the Third Market and I am engaging in a riskless principal trade consistent with the new trade-reporting rules, how do I confirm the transaction to my customer under SEC Rule 10b-10? For example, what would I have to confirm in the transaction described in the previous question?

As noted above in the text of this *Notice*, the SEC stated in its approval order of the rule that Exchange Act Rule 10b-10 requires a broker/dealer acting as Market Maker in a riskless principal transaction in an exchange-listed security to confirm to its customer:

1) the reported trade price;

2) the price to the customer in the transaction; and

3) and the difference, if any, between the reported trade price and the price to the customer (*i.e.*, any markup or markdown, commission equivalent, or other fee on top of the reported price).

The SEC further stated that under Rule 10b-10, the broker/dealer is required to report, as the reported trade price, the price at which the security was reported to the CTA when the member purchased the security for, or sold the security on behalf of, its customer. The Commission stated that this requirement remains in effect regardless of the fact that there is no corresponding requirement in the NASD rules to report the second leg of a riskless principal transaction to the tape.

For example, when a Market Maker receives an execution report from an exchange in a listed security through ITS and completes a riskless principal transaction by filling a customer order, the Market Maker must report on the confirmation to its customer the price of the transaction that was reported to the tape by the exchange (*i.e.*, the reported price). (The same would hold true if the transaction occurred in the Third Market between two Market Makers.) The Market Maker must also report the price to the customer and any markup or markdown or other fee charged by the Market Maker to the customer (*i.e.,* any difference between the price reported by the exchange and the price to the customer).

With regard to Question 12, where MMA sent a buy market order to the floor of an exchange and received a report back from the specialist of $20 1/4, first assume that MMA charges the customer no markup, commission equivalent, or other fee. In that case, MMA would confirm to the customer:

1) a reported trade price of $20 1/4 (the price reported by the exchange to CTA);

2) a price to the customer of $20 1/4; and

3) a no differential.

If MMA had added a commission equivalent of 1/4, MMA would have confirmed:

1) a trade price of $20 1/4 ;

2) a price to the customer of $20 1/2; and

3) a differential of 1/4.

Finally, for riskless principal trades effected by non-Market Makers trading as principal in the Third Market, SEC Rule 10b-10 confirmation requirements remain the same as they are today.

14. CQS Inside Market: $10 - 10 1/4, 10 X 10

MMA receives from an institutional customer an order to sell 100,000 shares with instructions to work the order with a price limit (or "bottom") of $10 1/16. MMA discloses that it will charge a commission equivalent of 1/16 on the trade. MMA sends a total of 25,000 shares (either through a single trade or multiple orders) to the floor of an exchange for execution, and MMA receives a report(s) back from the exchange of $10 1/8 per share. Instead of attempting to find the remaining

75,000 shares, MMA fills the entire customer order for 100,000 shares, for a price of $10 1/8 per share, by trading the 75,000-share balance out of inventory. How is this trade reported?

Only a portion of the 100,000 share transaction is deemed to be riskless – the 25,000 shares. The remaining 75,000 shares that were executed from MMA's inventory are considered to be "at risk," and must be reported to the tape. Thus, MMA reports only a buy of 75,000, and not a buy of 100,000 shares, from its institutional customer because the 75,000 is deemed to be "at risk" and the remaining 25,000 is deemed riskless and previously reported by the exchange. The confirmation to the customer would show a reported price of $10 1/8 (the price printed on the exchange and in the Third Market), a price to the customer of $10 1/16, and a differential (commission equivalent) of 1/16.

15. In the above example, it may not be easy for MMA to definitively say that 25,000 shares were riskless, because MMA may have accumulated these shares in multiple transactions that were reported back to MMA throughout the entire day. Can MMA still report these as riskless principal?

No. In order for a Market Maker to report trades as riskless principal, the Market Maker must be able to identify a specific trade or a group of trades (which may be effected at one price level or multiple price levels if the customer is receiving a volume weighted average price (VWAP)) as being those utilized to fill a customer order. If a member cannot identify which trade or series of trades were effected to offset a customer order, the Market Maker is at risk and cannot report as riskless principal.

Thus, in the previous question where MMA was claiming 25,000 shares were riskless principal, MMA must be able to tie a specific trade or trades to the 25,000 shares. If MMA were reporting a VWAP of $10 1/8 because MMA received multiple executions on a number of trades sent to the floor of an exchange, MMA would have to point to a series of transactions which had a volume weighted average price of $10 1/8 and which totaled 25,000 shares.

16. CQS Inside Market: $10 - 10 1/8, 10 X 10

After receiving a 5,000-share order to buy at $10, MMA places a marker order to buy 500 shares at $10 on an exchange. The marker order is executed and triggers the 5,000-share customer order. MMA then fills the 5,000-share customer order. What are MMA's trade-reporting obligations?

MMA would report the 5,000 shares in its entirety (not merely 4,500 shares) and would not exclude the 500 shares executed on and reported by the exchange, since the marker order represents only 10 percent of the 5,000-share order. As a variation of this example, assume the marker order triggers 10 different orders each to buy 500 shares at $10, for a total of 5,000 shares. Similarly, the Market Maker would report each of these 500-share (*i.e.*, a total of 10) trades with its customers.

17. CQS Inside Market: $10 - 10 1/8, 10 X 10

After receiving an order to buy 10,000 shares at $10, MMA places a marker order to buy 2,500 shares at $10 on an exchange. The marker order is executed and triggers the 10,000-share order. MMA then fills the 10,000-share customer order. What are MMA's trade-reporting obligations?

The Market Maker would report the 7,500 shares in the Third Market, and would not report the remaining 2,500-marker order executed on the exchange because that order is greater than 10 percent of the 10,000-share customer order and is otherwise riskless.

18. CQS Inside Market: $10 - 10 3/8, 10 X 10

MMA receives a not-held order from an institutional customer to sell 6,000 shares, with instructions to obtain the best price available with a "bottom" of $10 1/8. MMA sells in the Third Market 4,000 shares at $10 3/8 to MMB and 2,000 shares at $10 to MMC. MMA then buys 6,000 shares at $10 1/4 from its customer. What are MMA's trade-reporting obligations?

MMA must report to the tape the sell to MMB of 4,000 shares at $10 3/8 and the sell to MMC of 2,000 shares at $10. (Note that the VWAP for this trade is $10 1/4). MMA would not report the offsetting purchase from its customer. The NASD believes that it would be consistent with an SEC No-Action Letter regarding SEC Rule 10b-10 for MMA to disclose on the confirmation a reported price of $10 1/4 — the VWAP — instead of a reported price for each individual transaction.[3] The confirmation must contain a notation that the disclosed price is an average price, and must note that details regarding the actual prices are available to the customer upon request.[4] If the Market Maker charged a markdown, commission-equivalent, or other fee on top of the $10 1/4, it also would be permissible for the confirmation to disclose the fee as a single amount.

19. CQS Inside 10 - 10 1/4, 10 x 10

MMA receives a limit order from its customer to sell 5,000 shares at $10 1/16. Through its internal execution system, MMA immediately buys 5,000 shares from its customer at a price of $10 1/16. To reduce its inventory position, MMA subsequently sends a limit order to sell 3,000 shares at $10 1/16 (as principal) to the floor of an exchange or another Market Maker in the Third Market, where the order is filled. What are the reporting obligations here?

MMA would report to the tape that it bought from its customer 5,000 shares at $10 1/16. Additionally, MMA's sell limit order of 3,000 at $10 1/16 that was executed on the floor of the exchange would be reported by the exchange. (Note, if MMA had executed the sell limit order in the Third Market (instead of on the exchange) by, for example, hitting the bid of another Market Maker, MMA would report the sell to the tape.) Note that no part of this transaction constitutes a riskless principal trade because MMA did not have the other side (or a portion thereof) of the customer's buy limit order in hand when it provided the internal execution. Thus, MMA incurred the risk that the market would move against it before MMA could send the offsetting order to the floor of the exchange to reliquify.

20. CQS Inside Market: $10 - 10 1/4, 10 X 10

MMA receives an order to buy 10,000 shares at a limit price of $10 1/8 from Institutional Customer 1, and simultaneously receives an order to sell 10,000 shares at a limit price of $10 1/8 from Institutional Customer 2. MMA buys 10,000 shares from Institutional Customer 2 and sells 10,000 to Institutional Customer 1, both at $10 1/8. How is this reported?

MMA reports the sale to Institutional Customer 1 as riskless principal for 10,000 shares at $10 1/8, assuming that the trades were effected from MMA's market-making account. There will be no trade report for the buy from Institutional Customer 2. MMA will confirm the respective transactions to both customers consistent with SEC Rule 10b-10.

If transaction had been effected as a pure agency cross and the trades were not run through MMA's market-making or proprietary account, MMA would report the transaction as an agency cross, not as riskless principal.

21. CQS Inside Market: $10 - 10 1/4, 10 X 10

MMA receives an order to buy 100,000 shares at a limit price of $10 1/8 from Institutional Customer 1, and simultaneously receives an order to sell 75,000 shares at a limit price of $10 1/8 from Institutional Customer 2. MMA crosses 75,000 shares, and in order to fill the remainder of Institutional Customer 1, sells 25,000 shares at $10 1/8 to the customer. How is this trade reported?

MMA would submit a trade report indicating an agency cross of 75,000 shares since the trade was effected as agent and not through MMA's market-making account. MMA would submit a separate trade report that would indicate a sale of 25,000 shares at $10 1/8 as principal. Note that the confirmation to Institutional Customer 1 would indicate that the firm acted both as principal and agent, consistent with the SEC No-Action Letter.[5]

Attachment B – Text Of Rule Changes

(Note: New text is underlined; deletions are in brackets.)

4632. Transaction Reporting

(a)(1) through (a)(8) No Change

(9) All members shall append a trade report modifier as designated by the Association to transaction reports that reflect a price different from the current market when the execution is based on a prior reference point in time, which shall be accompanied by the prior reference time.

(b) through (f)(1)(C) No Change

(D) Orders received or initiated by the reporting member which are impractical to report individually and are executed at the same price within 60 seconds of execution of the initial transaction; provided however, that no individual order of 10,000 shares or more may be aggregated in a transaction report and that the aggregated transaction report shall be made within 90 seconds of the initial execution reported therein. Furthermore, it is not permissible for a member to withhold reporting a trade in anticipation of aggregating the transaction with other transactions. The limitation on aggregating individual orders of 10,000 shares or more for a particular security shall not apply on the first day of secondary market trading of an IPO for that security.

4642. Transaction Reporting

(a)(1) through (a)(8) No Change

(9) All members shall append a trade report modifier as designated by the Association to transaction reports that reflect a price different from the current market when the execution is based on a prior reference point in time, which shall be accompanied by the prior reference time.

(b) through (f)(1)(C) No Change

(D) Orders received or initiated by the reporting member which are impractical to report individually and are executed at the same price within 60 seconds of execution of the initial transaction; provided however, that no individual order of 10,000 shares or more may be aggregated in a transaction report and that the aggregated transaction report shall be made within 90 seconds of the initial execution reported therein. Furthermore, it is not permissible for a member to withhold reporting a trade in anticipation of aggregating the transaction with other transactions. The limitation on aggregating individual orders of 10,000 shares or more for a particular security shall not apply on the first day of secondary market trading of an IPO for that security.

4652. Transaction Reporting

(a)(1) through (a)(7) No Change

(8) All members shall append a trade report modifier as designated by the Association to transaction reports that reflect a price different from the current market when the execution is based on a prior reference point in time, which shall be accompanied by the prior reference time.

6420. Transaction Reporting

(a) through (c) No Change

(d) **Procedures for Reporting Price and Volume**

Members which are required to report pursuant to paragraph (b) above shall transmit last sale reports for all purchases and sales in eligible securities in the following manner:

(1) through (2) No Change

(3) (A) For principal transactions, except as provided below, report each purchase and sale transaction separately and report the number of shares and the price. For principal transactions which are executed at a price which includes a markup, markdown or service charge, the prices reported shall exclude the markup, markdown or service charge. [Such reported price shall be reasonably related to the prevailing market, taking into consideration all relevant circumstances including, but not limited to, market conditions with respect to the security, the number of shares involved in the transaction, the published bids and offers with size at the time of the execution (including the reporting firm's own quotation), accessibility to market centers publishing bids and offers with size, the cost of execution and the expenses involved in clearing the transaction.]

(B) Exception: A "riskless" principal transaction in which a member [that is not a market maker in the security] after having received from a customer an order to buy, purchases the security as principal from another member or customer to satisfy the order to buy or, after having received from a customer an order to sell, sells the security as principal to another member or customer to satisfy the order to sell, shall be reported as one transaction in the same manner as an agency transaction, excluding the markup or markdown. A riskless principal transaction in which a member purchases or sells the security on an exchange to satisfy a customer's order will be reported by the exchange and the member shall not report.

6620. Transaction Reporting

(a)(1) through (a)(5) No Change

(6) All members shall append a trade report modifier as designated by the Association to transaction reports that reflect a price different from the current market when the execution is based on a prior reference point in time, which shall be accompanied by the prior reference time.

Endnotes

[1]*See* Exchange Act Release No.16960, 45 FR 47291 (July 7, 1980) (approving SR-NASD-80-3).

[2]*See e.g.*, Exchange Act Release No. 40260, n. 63 and 67 (July 24, 1998), 63 FR 40748 (July 30, 1998) (proposed amendments to National Market System plan); Exchange Act Release No. 18713 (May 6, 1982) 47 FR 20413, n.13 (May 12, 1982) (adoption of final amendments to National Market System plan).

[3]*See, e.g.*, SEC No-Action Letter from Catherine McGuire, SEC, to Eugene Lopez, The Nasdaq Stock Market, dated May 6, 1997 (permitting the issuance of a single confirmation at an average price and with multiple capacities for a single customer order effected with multiple executions).

[4]*See id*.

[5]*See id*.

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NASD Notice to Members 99-67

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- ☐ Variable Contracts

Executive Summary

NASD Regulation, Inc. (NASD Regulation®) is proposing to amend the rules governing new member applications and applications for approval of a change in a member's ownership, control, or operations. The text of the proposed amendments is included with this *Notice to Members—Request For Comment* (see Attachment A). A detailed explanation of the proposed rules follows in Attachment B.

Request For Comment

NASD Regulation encourages all interested parties to comment on the proposal. Comments must be received by **September 13, 1999**. Comments should be mailed to:

Joan Conley
Office of the Corporate Secretary
NASD Regulation, Inc.
1735 K Street, NW
Washington, D.C. 20006-1500

or e-mailed to:
pubcom@nasd.com

Important Note: The only comments that will be considered are those submitted via e-mail or in writing.

Before becoming effective, any rule change developed as a result of comments received must be adopted by the NASD Regulation Board of Directors, may be reviewed by the National Association of Securities Dealers, Inc. (NASD®) Board of Governors, and must be approved by the Securities and Exchange Commission (SEC).

Questions/Further Information

As noted, written comments should be submitted to Joan Conley. Questions concerning this *Notice to Members—Request For Comment* may be directed to Mary M. Dunbar, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8252; or to Jeffrey S. Holik, Director of Regulation Policy, Member Regulation, NASD Regulation, at (202) 728-8387.

Changes To Membership Rules

NASD Regulation invites members to comment on amendments to the Rule 1010 Series, which govern NASD membership. NASD Regulation staff and the Member Admission Review Committee (Committee),[1] an ad-hoc committee convened in August 1998, developed the proposed changes. NASD Regulation asked the Committee to suggest ways to streamline the rules and make them more efficient while preserving their investor protection function. The Board, as well as the Membership Committee, the National Adjudicatory Council (NAC), and the Small Firm Advisory Board, approved the proposed changes.

The most significant changes are as follows:

- reorganizing and consolidating some of the current rules to make them easier to use;
- clarifying the rules and policies that apply to business expansions by—
  - adopting a policy of building expansion plans into membership agreements,
  - defining in the rules what kinds of "material changes in business operations" require a member to file an application for approval with NASD Regulation, and

- providing a safe harbor for modest expansions that will not require an application,

which together are intended to provide more even-handed treatment among members for various business expansions, provide more certainty regarding which expansions require approval, and eliminate unnecessary applications;

- simplifying administrative procedures for submitting an application and calculating the various time limits that apply to the process;

- rescinding the NAC's authority to review membership decisions that are not appealed by an applicant;

- permitting the staff to stay membership applications if a firm or one of its principals is the subject of a disciplinary action; and

- permitting the staff to reject immediately applications that are not substantially complete.

Attachment A

Text Of Amendments

(Note: New text is underlined; deletions are in brackets.)

1010. Membership Proceedings

1011. Definitions

Unless otherwise provided, terms used in the Rule 1010 Series shall have the meaning as defined in Rule 0120.

(a) "Applicant"

The term "Applicant" means a person [or entity] that applies for membership in the Association under Rule 1013[,] or a member that files an application [to remove or modify a restriction under Rule 1017, or files a notice and application for continuance in membership under Rule 1018] for approval of a change in ownership, control, or business operations under Rule 1017.

(b) "Associated Person"

The term "Associated Person" means: (1) a natural person registered under the Rules of the Association; or (2) a sole proprietor, partner, officer, director, branch manager, or other natural person occupying a similar status or performing similar functions who will be or is anticipated to be associated with the Applicant, or a natural person engaged in the investment banking or securities business who will be or is anticipated to be directly or indirectly controlling or controlled by the Applicant, whether or not any such person is registered or exempt from registration under the NASD By-Laws or the Rules of the Association.

(c) "Department"

The term "Department" means the Department of Member Regulation of NASD Regulation.

(d) "Director"

The term "Director" means a member of the NASD Regulation Board.

(e) "district"

The term "district" means a district established by the NASD Regulation Board.

(f) "district office"

The term "district office" means an office of NASD Regulation located in a district.

(g) "Governor"

The term "Governor" means a member of the NASD Board.

(h) "Interested Association Staff"

The term "Interested Association Staff" means an employee who directly participates in a decision under Rule 1014[,] or 1017, [or 1018,] an employee who directly supervises an employee with respect to such decision, an employee who conducted an investigation or examination of a member that files an application under Rule 1017 [or a notice and application under Rule 1018], the District Director for the relevant district, and the head of the Department.

(i) "material change in business operations"

The term "material change in business operations" includes, but is not limited to:

(1) removing or modifying a membership agreement restriction;

(2) adding a type of business listed in Item 12 of Form BD, regardless of the percentage of annual revenue expected to be generated by the activity;

(3) adding business activities that require a higher minimum net capital under SEC Rule 15c3-1;

(4) managing or co-managing for the first time: (A) a firm commitment underwriting; or (B) a conditional arrangement for the distribution of new securities, such as a best efforts commitment; unless the Association has given the member prior approval to act as manager or co-manager; or

(5) increasing the number of Associated Persons involved in sales or the number of offices or markets made in excess of any one or more of the safe harbors in Interpretive Material 1011-1.

[(i)] (j) "NASD Board"

The term "NASD Board" means the Board of Governors of the NASD.

[(j)](k) "NASD Regulation Board"

The term "NASD Regulation Board" means the Board of Directors of NASD Regulation.

(l) "principal place of business"

The term "principal place of business" means the executive office from which the sole proprietor or the officers, partners, or managers of the Applicant direct, control, and coordinate the activities of the Applicant, unless the Department determines that the principal place of business is where: (1) the largest number of Associated Persons of the

Applicant are located; or (2) the books and records necessary to provide information and data to operate the business and comply with applicable rules are located.

[(k)](m) "sales practice [violations] event"

The term "sales practice [violations] event" means any [conduct directed at or involving a customer that would constitute a violation of any Rule in the Rule 2000 or 3000; any provision of the Act, Securities Exchange Act of 1934; or any state statute prohibiting fraudulent conduct in connection with the offer, sale, or purchase of a security or in connection with the rendering of investment advice] customer complaint, arbitration, or civil litigation that has been reported to the Central Registration Depository, currently is required to be reported to the Central Registration Depository, or otherwise has been reported to the Association.

[(l)](n) "Subcommittee"

The term "Subcommittee" means a subcommittee of the National Adjudicatory Council that is constituted pursuant to Rule 1015 to conduct a review of a Department decision issued under the Rule 1010 Series.

IM-1011-1. Safe Harbors for Business Expansions

This interpretive material concerns the types of business expansions that will not require a member to submit a Rule 1017 application to obtain NASD Regulation's approval of the expansion. This safe harbor applies to: (1) firms that do not have a membership agreement, and (2) firms that have a membership agreement that does not contain a "restriction" on the factors listed below.

The safe harbor is not available to a member that has a membership agreement that contains a specific restriction as to one or more of the factors listed below. In that case, the agreement takes precedence because NASD Regulation has determined that a particular restriction should apply as to one or more of the factors, and NASD Regulation has issued a decision with a rationale for that restriction. Similarly, the safe harbor also does not apply if the member has a membership agreement that permits expansion beyond the limits set forth below (e.g., an Applicant requests and obtains approval for ten registered representatives in the first six months with an additional ten registered representatives in the next year); in such case, the Department has specifically considered the firm's expansion plans and approved them.

The safe harbor is not available to any member that has disciplinary history. For purposes of this Interpretation, "disciplinary history" means a finding of a violation in the past five years by the Securities and Exchange Commission, a self-regulatory organization, or a foreign financial regulatory authority of one or more of the following provisions (or a comparable foreign provision): Section 15(b)(4)(E) of the Securities Exchange Act of 1934; Section 17(a) of the Securities Act of 1933; SEC Rules 10b-5 and 15g-1 through 15g-9; NASD Rules 2110, 2120, 2310, 2330, 2440, 3010 (failure to supervise only), 3310, and 3330; and MSRB Rules G-19, G-30, and G-37(b) & (c).

For those firms to which the safe harbor is available, the following types of expansions are presumed not to be a material change in business operations and therefore do not require a Rule 1017 application. For any expansion beyond these limits, a member is required to contact its district office prior to implementing the change to determine whether the proposed expansion requires an application under Rule 1017. Expansions in each area are measured on a rolling 12-month basis; members are required to keep records of increases in personnel, offices, and markets to determine whether they are within the safe harbor.

"Associated Persons involved in sales" includes all Associated Persons, whether or not registered, who are involved in sales activities with public customers, including sales assistants and cold callers, but excludes clerical, back office, and trading personnel who are not involved in sales activities.

Number of Associated Persons Involved in Sales	**Safe Harbor – Increase Permitted Within One Year Period Without Rule 1017 Application**
1-10	10 persons
11 or more	10 persons or a 30 percent increase, whichever is greater

Number of Offices (registered or unregistered)	
1-5	3 offices
6 or more	3 offices or a 30 percent increase, whichever is greater
Number of Markets Made	
1-10	10 markets
11 or more	10 markets or a 30 percent increase, whichever is greater

1012. General Provisions

(a) [Service of Notices and Decisions;] Filing by Applicant or Service by the Association

[A notice or a decision issued by the Association under the Rule 1010 Series with respect to an application shall be served promptly by first-class mail on the Applicant or its counsel, unless a Rule specifies a different method of service. Service by the Association or filing by an Applicant by mail shall be deemed complete upon mailing. Service by the Association or filing by an Applicant by commercial courier or facsimile shall be deemed complete on the date specified in the written confirmation of receipt.]

(1) An Applicant may file an application or any document or information requested under the Rule 1010 Series by first-class mail, overnight courier, or hand delivery. If the Department and the Applicant agree, the Applicant also may file a requested document or information by facsimile.

(2) The Association shall serve a notice or decision issued under the Rule 1010 Series by first-class mail on the Applicant or its counsel, unless a Rule specifies a different method of service.

(3) Service by the Association or filing by an Applicant shall be deemed complete as follows:

(A) Service or filing by first-class mail shall be deemed complete on the date of postmark;

(B) Service or filing by overnight courier shall be deemed complete on the date of delivery to the overnight courier as specified in the airbill;

(C) Service or filing by hand delivery shall be deemed complete on the date of receipt as evidenced by a date stamp; and

(D) Service or filing by facsimile shall be deemed complete on the date specified in the document and on the written confirmation of transmission.

(b) Lapse of Application

(1) Absent a showing of good cause, an application filed under Rule 1013 or 1017 shall lapse if an Applicant fails to:

(A) respond fully within 60 days after service of an initial written request for information or documents under Rule 1013, within 30 days after service of an initial written request for information or documents under Rule 1017, within 30 days after service of a subsequent written request for information or documents under Rule 1013 or 1017, or within such other time period agreed to by the Department and the Applicant;

(B) appear at or otherwise participate in a scheduled membership interview pursuant to Rule 1013(b) or 1017(f); or

(C) file an executed membership agreement under Rule 1014(d) or Rule 1017(g)(4) within 25 days after service of the agreement, or within such other time period agreed to by the Department and the Applicant.

(2) If an Applicant wishes to continue to seek membership or approval of a change in ownership, control, or business operations, then the Applicant shall be required to submit a new application and fee under Rule 1013 or 1017, respectively. The Association

shall not refund any fee for a lapsed application.

[(b)] (c) Ex Parte Communications

(1) The prohibitions against ex parte communications shall become effective when Association staff has knowledge that an Applicant intends to file a written request for review by the National Adjudicatory Council under Rule 1015.

[(1)] (2) Unless on notice and opportunity for an Applicant and Interested Association Staff to participate, or to the extent required for the disposition of ex parte matters as authorized by the Rules of the Association:

(A) an Applicant, a counsel or representative of an Applicant, or an Interested Association Staff shall not make or knowingly cause to be made an ex parte communication relevant to the merits of a membership proceeding under the Rule 1010 Series to a Governor, a member of the National Adjudicatory Council or a Subcommittee thereof, or an Association employee who is participating or advising in a decision of such a person with respect to that proceeding; and

(B) a Governor, a member of the National Adjudicatory Council or a Subcommittee thereof, or an Association employee who is participating or advising in the decision of such a person with respect to a membership proceeding shall not make or knowingly cause to be made to an Applicant, a counsel or representative of the Applicant, or an Interested Association Staff an ex parte communication relevant to the merits of that proceeding.

[(2)] (3) A Governor, a member of the National Adjudicatory Council or a Subcommittee thereof, or an Association employee participating or advising in the decision of such a person, who receives, makes, or knowingly causes to be made a communication prohibited by this paragraph shall place in the record of the membership proceeding:

(A) all such written communications;

(B) memoranda stating the substance of all such oral communications; and

(C) all written responses and memoranda stating the substance of all oral responses to all such communications.

[(3) The prohibitions against ex parte communications shall become effective when Association staff has knowledge that an Applicant intends to file a written request for review by the National Adjudicatory Council under Rule 1015.]

[(c)] (d) Recusal or Disqualification

A Governor or a member of the National Adjudicatory Council or a Subcommittee thereof shall not participate in a matter governed by the Rule 1010 Series as to which that person has a conflict of interest or bias, or if circumstances otherwise exist where his or her fairness might reasonably be questioned. In such a case, the person shall recuse himself or shall be disqualified as follows:

(1) The Chair of the NASD Board shall have authority to direct the disqualification of a Governor, and a majority of the Governors of the NASD Board excluding the Chair shall have authority to direct the disqualification of the Chair of the NASD Board.

(2) The Chair of the National Adjudicatory Council shall have authority to direct the disqualification of a member of the National Adjudicatory Council or a member of a Subcommittee appointed pursuant to Rule 1015, and the Vice Chair of the National Adjudicatory Council shall have authority to direct the disqualification of the Chair of the National Adjudicatory Council.

[(d)] (e) Computation of Time

(1) Calendar Day

In the Rule 1010 Series, “day” means calendar day.

(2) Formula

In computing a period of time under the Rule 1010 Series, the day of the act, event, default, or lapse from which the period of time designated begins to run shall not be included. The last day of the period so computed shall be included unless it is a Saturday, Sunday, or Federal holiday, in which event the period runs until the end of the next day that is not a Saturday, Sunday, or Federal holiday. Intermediate Saturdays, Sundays, and Federal holidays shall be excluded from the computation when the period prescribed is ten days or less.

1013. New Member Application [and Membership] and Interview

(a) Filing of Application

(1) Where To File

[Each Applicant for Association membership shall file its application in two parts. The first part of the application shall be filed with the Membership Department and shall include the following documents:]

An Applicant for Association membership shall file its application with the Department of Member Regulation at the district office in the district in which the Applicant intends to have its principal place of business as defined in Rule 1011(l).

(2) Contents

The application shall include:

(A) an original signed and notarized Form BD, with applicable schedules;

(B) an original signed Form U-4 for each Associated Person who is required to be registered under the Rules of the Association;

(C) an original NASD-approved fingerprint card for each Associated Person who will be subject to SEC Rule 17f-2;

(D) a new member assessment report;

[(E) a new member firm contact questionnaire; and]

[(F)] (E) a check for the appropriate fee[.];

[(2) The second part of the application shall be filed with the Department of Member Regulation at the district office in the district in which the Applicant intends to have its principal place of business and shall include the following information and documents:]

[(A)] (F) a detailed business plan[, in a form prescribed by the Association,] that adequately and comprehensively describes all material aspects of the business that will be, or are reasonably anticipated to be, performed at and after the initiation of business operations, including future business expansion plans, if any, and includes:

(i) a trial balance, balance sheet, supporting schedules, and computation of net capital, each of which has been prepared as of a date that is within 30 days before the filing date of the application;

(ii) a monthly projection of income and expenses, with a supporting rationale, for the first twelve months of operations;

(iii) an organizational chart;

(iv) [a list of] the intended [locations] location of [all offices,] the Applicant's principal place of business and all other offices, if any, whether or not such offices would be required to be registered under the Rules of the Association, and the names of the persons who will be in charge of each office;

(v) a list of the types of securities to be offered and sold and the types of retail or institutional customers to be solicited;

(vi) a description of the methods and media to be employed to develop a customer base and to offer and sell products and services to customers, including the use of the Internet, telephone solicitations, seminars, or mailings;

(vii) a description of the business facilities and a copy of any proposed or final lease;

(viii) the number of markets to be made, if any, the type and volatility of the products, and the anticipated maximum inventory positions;

(ix) any plan to enter into contractual commitments, such as underwritings or other securities-related activities;

(x) any plan to distribute or maintain securities products in proprietary positions, and the risks, volatility, degree of liquidity, and speculative nature of the products; [and]

(xi) any other activity that the Applicant may engage in that reasonably could have a material impact on net capital within the first twelve months of business operations; and

(xii) a description of the communications and operational systems the Applicant will employ to conduct business with customers or other members and the plans and procedures the Applicant will employ to ensure business continuity, including: system

capacity to handle the anticipated level of usage; contingency plans in the event of systems or other technological or communications problems or failures that may impede customer usage or firm order entry or execution; system redundancies; disaster recovery plans; system security; disclosures to be made to potential and existing customers who may use such systems; and supervisory or customer protection measures that may apply to customer use of, or access to, such systems;

[(B) a copy of the Applicant's most recent Form BD;]

[(C)](G) a copy of any decision or order by a federal or state authority or self-regulatory organization taking permanent or temporary adverse action with respect to a registration or licensing determination regarding the Applicant or an Associated Person;

[(D)](H) a list of all Associated Persons[, the most recent Form U-4 and Form U-5 for each Associated Person, any other document that discloses the disciplinary history of each Associated Person, and a list of any other persons or entities that will exercise control with respect to the Applicant's business];

[(E)](I) documentation of any of the following events, unless the event has been reported to the Central Registration Depository:

(i) a regulatory action against or investigation of the Applicant or an Associated Person by the Commission, the Commodity Futures Trading Commission, a federal, state, or foreign regulatory agency, or a self-regulatory organization that is pending, adjudicated, or settled;

(ii) an investment-related civil action for damages or an injunction against the Applicant or an Associated Person that is pending, adjudicated, or settled;

(iii) an investment-related customer complaint or arbitration [involving sales practice violations, theft, misappropriation, conversion, or breach of fiduciary duty, against the Applicant or an Associated Person that is pending, settled, or has resulted in an award or judgement] that is required to be reported on Form U-4; [and]

(iv) a criminal action (other than a minor traffic violation) against the Applicant or an Associated Person that is pending, adjudicated, or that has resulted in a guilty or no contest plea; and

[(F)](v) a copy of any document evidencing a termination for cause or a permitted resignation after investigation of an alleged violation of a federal or state securities law, a rule or regulation thereunder, a self-regulatory organization rule, or an industry standard of conduct;

[(G)](J) a description of any remedial action, such as special training [or], continuing education requirements, or heightened supervision, imposed on an Associated Person by a state or federal authority or self-regulatory organization;

[(H)](K) a written acknowledgment that heightened supervisory procedures and special educational programs may be required pursuant to Notice To Members 97-19 for an Associated Person whose record[s] reflects[:

(i)] disciplinary actions [involving] or sales practice [violations] events;

[(ii) customer complaints; or

(iii) arbitrations that were resolved adversely to the Associated Person;]

[(I)](L) a copy of final or proposed contracts with banks, clearing entities, or service bureaus, and a general description of any other final or proposed contracts;

[(J)](M) a description of the nature and source of Applicant's capital with supporting documentation, including a list of all persons or entities that have contributed or plan to contribute financing to the Applicant's business, the terms and conditions of such financing arrangements, the risk to net capital presented by the Applicant's proposed business activities, and any arrangement for additional capital should a business need arise;

[(K)](N) a description of the financial controls to be employed by the Applicant;

[(L)](O) a description of the Applicant's supervisory system and a copy of its written supervisory procedures, internal operating procedures (including operational and internal controls), internal inspections plan, written approval process, and qualifications investigations required by Rule 3010;

[(M)](P) a description of the number, experience, and qualifications of supervisors and principals and the number, experience, and qualifications of persons to be supervised by such personnel, the other responsibilities of the supervisors and principals with the Applicant, their full-time or part-time status, any business activities that the supervisors or principals may engage in outside of their association with the Applicant, the hours per week devoted to such activities, and an explanation of how a part-time supervisor or principal will be able to discharge his or her designated functions on a part-time basis;

[(N)](Q) a description of Applicant's proposed recordkeeping system; and

[(O)](R) a copy of the Applicant's written training plan to comply with Firm Element continuing education requirements described in Rule 1120(b), including the name of the Associated Person responsible for implementation[; and]

[(P) a copy of the documents described in paragraph (a)(1)].

(3) Electronic Firm Contact Questionnaire [The Applicant shall file both parts of the application simultaneously by commercial courier. The application shall be deemed received on the date specified in the written confirmation of receipt generated by the commercial courier for the delivery of the second part of the application to the district office.] The Applicant also shall submit an electronic firm contact questionnaire, including its electronic mail address.

(4) Rejection Of Application That Is Not Substantially Complete

If the Department determines within 30 days after the filing of an application that the application is not substantially complete, the Department may reject the application and deem it not to have been filed. In such case, within the 30 day period, the Department shall serve a written notice on the Applicant of the Department's determination and the reasons therefor. The Association shall refund the application fee, less $350, which shall be retained by the Association as a processing fee. If the Applicant determines to continue to seek membership, the Applicant shall submit a new application and fee under this Rule.

(5) Request For Additional Documents Or Information

Within 30 days after the [receipt] filing of an application, the Department shall [determine whether the application is complete and, if not, shall request] serve an initial request for any additional information or documents necessary to render a decision on the application. The Department may [request] serve subsequent requests for additional information or documents at any time during the membership application process.

[(5)] Unless otherwise agreed by the Department and the Applicant, the Applicant shall file any additional information and documents with the Department within 60 days after service of the Department's initial request and 30 days after service of any subsequent request.

[(b) Lapse of Application]

[(1) Absent a showing of good cause, an application for membership shall lapse if an Applicant fails to:

(A) respond fully within 60 days after an initial request for information or documents, within 30 after any subsequent request, or within such other time period agreed to by the Department and the Applicant;

(B) appear at or otherwise participate in a scheduled membership interview pursuant to paragraph (c); or

(C) return an executed membership agreement under Rule 1014(c) within 25 days after service of the agreement.]

[(2) The lapse of an application shall require an Applicant continuing to seek membership to submit a new application under paragraph (a).]

[(c)](b) Membership Interview

(1) Requirement for Interview

Before the Department [issues

a] serves its decision on an application for new membership in the Association, the Department shall conduct a membership interview with a representative or representatives of the Applicant.

(2) Service of Notice

At least seven days before the membership interview, the Department shall serve on the Applicant a written notice that specifies the date and time of the interview and the representative or representatives of the Applicant who are required to participate in the interview. The Department shall serve the notice by facsimile or commercial courier. The Applicant and the Department may agree to a shorter or longer period for notice or a different method of service under this subparagraph.

(3) Time

Unless the Department directs otherwise for good cause shown, a membership interview shall be scheduled to occur within 90 days after the [receipt] filing of an application or within 60 days after the [receipt] filing of all additional information or documents requested, whichever is later.

(4) Place

Unless the Department and the Applicant otherwise agree, the membership interview shall be conducted in the district office for the district in which the Applicant has or intends to have its principal place of business.

(5) Updated Financial Documents

On or before the date of the membership interview, the Applicant shall file an updated trial balance, balance sheet, supporting schedules, and computation of net capital. The Applicant shall prepare such documents as of a date that is within 45 days before the date of the membership interview, unless the Applicant and the Department agree on a longer period. The Applicant shall promptly notify the Department in writing of any material adverse change in its financial condition that occurs before a decision constituting final action of the Association is served on the Applicant.

[(5)](6) Review of Standards for Admission

During the membership interview, the Department shall review the application and the standards for admission to membership with the Applicant's representative or representatives.

[(6)](7) Information From Other Sources

During the membership interview, the Department shall provide to the Applicant's representative or representatives any information or document that the Department has obtained from the Central Registration Depository or a source other than the Applicant and upon which the Department intends to base its decision under Rule 1014. If the Department receives such information or document after the membership interview or decides to base its decision on such information after the membership interview, the Department shall promptly serve the information or document and an explanation thereof on the Applicant.

1014. Department Decision

(a) Standards for Admission

After considering the application, the membership interview, other information and documents provided by the Applicant, other information and documents obtained by the Department, and the public interest and the protection of investors, the Department shall determine whether the Applicant meets each of the following standards:

(1) The application and all supporting documents are complete and accurate.

(2) The Applicant and its Associated Persons have all licenses and registrations required by state and federal authorities and self-regulatory organizations.

(3) The Applicant and its Associated Persons are capable of complying with the federal securities laws, the rules and regulations thereunder, and the Rules of the Association, including observing high standards of commercial honor and just and equitable principles of trade. In determining whether this standard is met, the Department may take into consideration whether:

(A) a state or federal authority or self-regulatory organization has taken permanent or temporary adverse action with respect to a registration or licensing determination regarding the Applicant or an Associated Person;

(B) an Applicant's or Associated Person's record[s] reflects[: (i) disciplinary actions involving sales practice violations; (ii)

customer complaints; or (iii) arbitrations that were resolved adversely to the Applicant or Associated Person] a sales practice event;

(C) an Applicant or Associated Person is the subject of a pending, adjudicated, or settled regulatory action or investigation by the Commission, the Commodity Futures Trading Commission, a federal, state, or foreign regulatory agency, or a self-regulatory organization; a pending, adjudicated, or settled investment-related civil action for damages or an injunction; [an investment-related customer complaint or arbitration alleging sales practice violations, theft, misappropriation, conversion, or breach of fiduciary duty that is pending, settled, or has resulted in an award or judgment;] or a criminal action (other than a minor traffic violation) that is pending, adjudicated, or that has resulted in a guilty or no contest plea;

(D) an Associated Person was terminated for cause or permitted to resign after an investigation of an alleged violation of a federal or state securities law, a rule or regulation thereunder, a self-regulatory organization rule, or industry standard of conduct;

(E) a state or federal authority or self-regulatory organization has imposed a remedial action, such as special training [or], continuing education requirements, or heightened supervision, on an Associated Person; and

(F) a state or federal authority or self-regulatory organization has provided information indicating that the Applicant or an Associated Person otherwise poses a threat to public investors.

(4) The Applicant has established all contractual or other arrangements and business relationships with banks, clearing corporations, service bureaus, or others necessary to: (A) initiate the operations described in the Applicant's business plan, considering the nature and scope of operations and the number of personnel; and (B) comply with the federal securities laws, the rules and regulations thereunder, and the Rules of the Association.

(5) The Applicant has or has adequate plans to obtain facilities that are sufficient to: (A) initiate the operations described in the Applicant's business plan, considering the nature and scope of operations and the number of personnel; and (B) comply with the federal securities laws, the rules and regulations thereunder, and the Rules of the Association.

(6) The communications and operational systems that the Applicant intends to employ for the purpose of conducting business with customers and other members are adequate and provide reasonably for business continuity in each area set forth in Rule 1013(a)(2)(F)(xii);

[(6)](7) The Applicant is capable of maintaining a level of net capital in excess of the minimum net capital requirements set forth in SEC Rule 15c3-1 adequate to support the Applicant's intended business operations on a continuing basis, based on information [that is current within 30 days before the membership interview] filed under Rule 1013(b)(5). The Department may impose a reasonably determined higher net capital requirement for the initiation of operations after considering:

(A) the amount of net capital sufficient to avoid early warning level reporting requirements, such as SEC Rule 17a-11;

(B) the amount of capital necessary to meet expenses net of revenues for at least twelve months, based on reliable projections agreed to by the Applicant and the Department;

(C) any planned market making activities, the number of markets to be made, the type and volatility of products, and the anticipated maximum inventory positions;

(D) any plan to enter into other contractual commitments, such as underwritings or other securities-related activities;

(E) any plan to distribute or maintain securities products in proprietary positions, and the risks, volatility, degree of liquidity, and speculative nature of the products; and

(F) any other activity that the Applicant will engage in that reasonably could have a material impact on net capital within the first twelve months of business operations.

[(7)](8) The Applicant has financial controls to ensure compliance with the federal securities laws, the rules and regulations thereunder, and the Rules of the Association.

[(8)](9) The Applicant has compliance, supervisory, operational, and internal control practices and standards that are consistent with practices and standards regularly employed in the investment banking or securities business, taking into account the nature and scope of Applicant's proposed business.

[(9)](10) The Applicant has a supervisory system, including written supervisory procedures, internal operating procedures (including operational and internal controls), and compliance procedures designed to prevent and detect, to the extent practicable, violations of the federal securities laws, the rules and regulations thereunder, and the Rules of the Association. In evaluating the adequacy of a supervisory system, the Department shall consider the overall nature and scope of the Applicant's intended business operations and shall consider whether:

(A) the number, location, experience, and qualifications of supervisory personnel are adequate in light of the number, location, experience, and qualifications of persons to be supervised; the [disciplinary history of such] Central Registration Depository record of supervisory personnel and persons to be supervised; [any criminal, civil, administrative, or arbitration actions or written customer complaints against such persons;] and the number and locations of the offices that the Applicant intends to open and the nature and scope of business to be conducted at each office;

(B) the Applicant has identified specific Associated Persons to supervise and discharge each of the functions in Applicant's business plan, and to supervise each of the Applicant's intended offices, whether or not such offices are required to be registered under the Rules of the Association;

(C) the Applicant has identified the functions to be performed by each Associated Person and has adopted procedures to assure the registration with the Association and applicable states of all persons whose functions are subject to such registration requirements.

[(C)] (D) each Associated Person identified in the business plan to discharge a supervisory function [in the business plan] has at least one year of direct experience or two years of related experience in the subject area to be supervised;

[(D)] (E) the Applicant will solicit retail or institutional business;

[(E)] (F) the Applicant will recommend securities to customers;

[(F)] (G) the location or part-time status of a supervisor or principal will affect such person's ability to be an effective supervisor;

[(G)] (H) [the records of an Associated Person reflect: (i) disciplinary actions involving sales practice violations; (ii) customer complaints; or (iii) arbitrations that were resolved adversely to the Associated Person] the Applicant should be required to place one or more Associated Persons under heightened supervision pursuant to Notice To Members 97-19;

[(H)] (I) any remedial action, such as special training or continuing education requirements or heightened supervision, has been imposed on an Associated Person by a state or federal authority or self-regulatory organization; and

[(I)] (J) any other condition that will have a material impact on the Applicant's ability to detect and prevent violations of the federal securities laws, the rules and regulations thereunder, and the Rules of the Association.

[(10)](11) The Applicant has a recordkeeping system that enables Applicant to comply with federal, state, and self-regulatory organization recordkeeping requirements and a staff that is sufficient in qualifications and number to prepare and preserve required records.

[(11)](12) The Applicant has completed a training needs assessment and has a written training plan that complies with the continuing education requirements imposed by the federal securities laws, the rules and regulations thereunder, and the Rules of the Association.

[(12)](13) The Association does not possess any information indicating that the Applicant may circumvent, evade, or otherwise avoid compliance with the federal securities laws, the rules and regulations thereunder, or the Rules of the Association.

[(13)](14) The application and all supporting documents otherwise are consistent with the federal securities laws, the rules and regulations thereunder, and the Rules of the Association.

(b) Granting or Denying Application

(1) If the Department determines that the Applicant meets each of the standards in paragraph (a), the Department shall grant the application for membership.

(2) If the Department determines that the Applicant does not meet one or more of the standards in paragraph (a) in whole or in part, the Department may:

(A) grant the application subject to one or more restrictions reasonably designed to address a specific financial, operational, supervisory, disciplinary, investor protection, or other regulatory concern based on the standards for admission in Rule 1014(a); or

(B) deny the application.

[(c) Submission of Membership Agreement

If the Department grants an application, with or without restriction, the Applicant's approval for membership shall be contingent upon the Applicant's submission of a written membership agreement, satisfactory to the Department, undertaking to:

(1) engage only in the business set forth in the business plan and the membership agreement;

(2) abide by any restriction specified in the Department's decision;

(3) obtain the Department's prior approval of the removal or modification of such a restriction pursuant to Rule 1017; and

(4) notify and obtain the Department's approval of a change in ownership or control or a material change in business operations pursuant to Rule 1018.

The Applicant shall not waive the right to file a written request for review under Rule 1015 by executing a membership agreement under this paragraph.]

[(d)] (c) Decision

(1) Time

The Department shall [issue] serve a written decision on the membership application within 30 days after the conclusion of the membership interview or after the [submission] filing of additional information or documents, whichever is later.

(2) Content

If the Department denies the application, the decision shall explain in detail the reason for denial, referencing the applicable standard or standards in paragraph (a). If the Department grants the application subject to restrictions, the decision shall explain in detail the reason for each restriction, referencing the applicable standard or standards in paragraph (a) upon which the restriction is based and identify the specific financial, operational, supervisory, disciplinary, investor protection, or other regulatory concern that the restriction is designed to address and the manner in which the restriction is reasonably designed to address the concern.

(3) Failure to [Issue] Serve Decision

If the Department fails to [issue] serve a decision within 180 days after [receipt] the filing of an application or such later date as the Department and the Applicant have agreed in writing, the Applicant may file a written request with the NASD Board requesting that the NASD Board direct the Department to [issue] serve a decision. Within seven days after [receipt] the filing of such a request, the NASD Board shall direct the Department to serve its written decision immediately or to show good cause for an extension of time. If the Department shows good cause for an extension of time, the NASD Board may extend the 180 day time limit by not more than 90 days.

(d) Submission of Membership Agreement

If the Department grants an application, with or without restriction, the Applicant's approval for membership shall be contingent upon the Applicant's filing of an executed written membership agreement, satisfactory to the Department, undertaking to:

(1) abide by any restriction specified in the Department's decision; and

(2) obtain the Department's approval of a change in ownership, control, or business operations pursuant to Rule 1017, including the modification or removal of a membership agreement restriction.

The Applicant shall not waive the right to file a written request for review under Rule 1015 by executing a membership agreement under this paragraph.

(e) Service and Effectiveness of Decision

The Department shall serve its decision and the membership agreement on the Applicant in accordance with Rule 1012. The decision shall become effective upon service and shall remain in effect during the pendency of any review until a decision constituting final action of the Association is issued under Rule 1015 or 1016, unless otherwise directed by the National Adjudicatory Council, the NASD Board, or the Commission.

(f) Effectiveness of Restriction

A restriction imposed under this Rule shall remain in effect and bind the Applicant and all successors to the ownership or control of the Applicant unless:

(1) removed or modified by [the Department under Rule 1017] a decision constituting final action of the Association issued under Rule 1015, 1016, or 1017;

[(2) removed or modified by a decision constituting final action of the Association issued under Rule 1015 or 1016;] or

[(3)](2) stayed by the National Adjudicatory Council, the NASD Board, or the Commission.

(g) Final Action

Unless the Applicant files a written request for a review under Rule 1015, the Department's decision shall constitute final action by the Association.

1015. Review by National Adjudicatory Council

(a) Initiation of Review by Applicant

[(1) Request by Applicant]

Within 25 days after service of a decision under Rule 1014[,] or 1017 [or 1018], an Applicant may file a written request for review with the National Adjudicatory Council. A request for review shall state with specificity why the Applicant believes that the Department's decision is inconsistent with the membership standards set forth in Rule 1014, or otherwise should be set aside, and state whether a hearing is requested. The Applicant simultaneously shall [send] file by first-class mail a copy of the request to the district office where the Applicant filed its [membership] application.

[(2) Notice by National Adjudicatory Council

A decision issued under Rule 1014, 1017, or 1018 shall be subject to a call for review by any member of the National Adjudicatory Council or the Review Subcommittee defined in Rule 9120 within 30 days after service of the decision. If the National Adjudicatory Council calls a decision for review, a written notice of review shall be served promptly on the Applicant by first-class mail. The written notice of review shall state the specific grounds for the review and whether a hearing is directed. If a decision is called for review by any member of the National Adjudicatory Council or the Review Subcommittee, the decision shall be reviewed by the National Adjudicatory Council. The National Adjudicatory Council simultaneously shall send by first-class mail a copy of the notice to the district office where the Applicant filed its membership application.]

(b) Transmission of Documents

Within ten days after [receipt] the filing of a request for [or notice of] review, the Department shall:

(1) transmit to the National Adjudicatory Council copies of all documents that were considered in connection with the Department's decision and an index to the documents; and

(2) serve on the Applicant a copy of such documents (other than those documents originally submitted by Applicant) and a copy of the index.

(c) Membership Application Docket

The Department shall promptly record in the Association's membership application docket each request for [or notice of] review filed with the National Adjudicatory Council under this Rule and each material subsequent event, filing, and change in the status of a membership proceeding.

(d) Appointment of Subcommittee

The National Adjudicatory Council or the Review Subcommittee defined in Rule 9120 shall appoint a Subcommittee to participate in the

review. The Subcommittee shall be composed of at least two members. One member shall be a current member of the National Adjudicatory Council. The remaining member or members shall be current or past Directors or past Governors.

(e) Powers of Subcommittee

If a hearing is requested [or directed], the Subcommittee shall conduct the hearing. If a hearing is not requested, the Subcommittee may serve a notice directing that a hearing be held. If a hearing is not requested or directed, the Subcommittee shall conduct its review on the basis of the record developed before the Department and any written submissions made by the Applicant or the Department in connection with the request for review.

(f) Hearing

(1) Notice

If a hearing is requested or directed, the hearing shall be held within 45 days after the [receipt] filing of the request [or service of the notice by] with the National Adjudicatory Council or service of the notice by the Subcommittee. The National Adjudicatory Council shall [send] serve written notice of the date and time of the hearing to the Applicant by facsimile or [commercial] overnight courier not later than 14 days before the hearing.

(2) Counsel

The Applicant and the Department may be represented by counsel at a hearing conducted pursuant to this Rule.

(3) Evidence

Formal rules of evidence shall not apply to a hearing under this Rule. Not later than five days before the hearing, the Applicant and the Department shall exchange copies of their proposed hearing exhibits and witness lists and provide copies of the same to the National Adjudicatory Council. If the Applicant or the Department fails to provide copies of its proposed hearing exhibits or witness list within such time, the Subcommittee shall exclude the evidence or witnesses from the proceeding, unless the Subcommittee determines that good cause is shown for failure to comply with the production date set forth in this subparagraph.

(4) Transcript

The hearing shall be recorded and a transcript prepared by a court reporter. A transcript of the hearing shall be available for purchase from the court reporter at prescribed rates. The Applicant, the Department, or a witness may seek to correct the transcript. A proposed correction of the transcript shall be submitted to the Subcommittee within a reasonable period of time prescribed by the Subcommittee. Upon notice to the Applicant and the Department, the Subcommittee may direct the correction to the transcript as requested or sua sponte.

[(5) Failure to Appear at Hearing]

[If an Applicant fails to appear at a hearing for which it has notice, the National Adjudicatory Council may dismiss the request for review as abandoned, and the decision of the Department shall become the final action of the Association. Upon a showing of good cause, the National Adjudicatory Council may withdraw a dismissal entered pursuant to this subparagraph.]

(g) Additional Information, Briefs

At any time during its consideration, the Subcommittee or the National Adjudicatory Council may direct the Applicant or the Department to [submit] file additional information [and to file] or briefs. Any additional information or brief [submitted] filed shall be provided to all parties before the National Adjudicatory Council renders its decision.

(h) Abandonment of Request for Review

If an Applicant fails to specify the grounds for its request for review under Rule 1015(a)(1), appear at a hearing for which it has notice, or file information or briefs as directed, the National Adjudicatory Council or the Review Subcommittee may dismiss the request for review as abandoned, and the decision of the Department shall become the final action of the Association. Upon a showing of good cause, the National Adjudicatory Council or the Review Subcommittee may withdraw a dismissal entered pursuant to this subparagraph.

[(h)] (i) Subcommittee Recommendation

The Subcommittee shall present a recommended decision in writing to the National Adjudicatory Council within 60 days after the date of the hearing held pursuant to paragraph (f), and not later than seven days before the meeting of the National Adjudicatory Council at which the membership proceeding shall be considered.

[(i)](j) Decision

(1) Proposed Written Decision

After considering all matters presented in the review and the Subcommittee's recommended written decision, the National Adjudicatory Council may affirm, modify, or reverse the Department's decision or remand the membership proceeding with instructions. The National Adjudicatory Council shall prepare a proposed written decision pursuant to subparagraph (2).

(2) Contents

The decision shall include:

(A) a description of the Department's decision, including its rationale;

(B) a description of the principal issues raised in the review;

(C) a summary of the evidence on each issue; and

(D) a statement whether the Department's decision is affirmed, modified, or reversed, and a rationale therefor that references the applicable standards in Rule 1014.

(3) Issuance of Decision After Expiration of Call for Review Periods

The National Adjudicatory Council shall provide its proposed written decision to the NASD Board. The NASD Board may call the membership proceeding for review pursuant to Rule 1016. If the NASD Board does not call the membership proceeding for review, the proposed written decision of the National Adjudicatory Council shall become final. The National Adjudicatory Council shall serve the Applicant with a written notice specifying the date on which the call for review period expired and stating that the final written decision will be served within 15 days after such date. The National Adjudicatory Council shall serve its final written decision within 15 days after the date on which the call for review period expired. The decision shall constitute the final action of the Association for purposes of SEC Rule 19d-3, unless the National Adjudicatory Council remands the membership proceeding.

(4) Failure to Issue Decision

If the National Adjudicatory Council fails to serve its final written decision within the time prescribed in subparagraph (3), the Applicant may file a written request with the NASD Board requesting that the NASD Board direct the National Adjudicatory Council to serve its decision immediately or to show good cause for an extension of time. Within seven days after [receipt] the filing of such a request, the NASD Board shall direct the National Adjudicatory Council to serve its written decision immediately or to show good cause for an extension of time. If the National Adjudicatory Council shows good cause for an extension of time, the NASD Board may extend the 15 day time limit by not more than 15 days.

1016. Discretionary Review by NASD Board

(a) Call for Review by Governor

A Governor may call a membership proceeding for review by the NASD Board if the call for review is made within the period prescribed in [sub]paragraph [(2)] (b).

(b) 15 Day Period; Waiver

A Governor shall make his or her call for review at the next meeting of the NASD Board that is at least 15 days after the date on which the NASD Board receives the proposed written decision of the National Adjudicatory Council. By unanimous vote of the NASD Board, the NASD Board may shorten the period to less than 15 days. By an affirmative vote of the majority of the NASD Board then in office, the NASD Board may, during the 15 day period, vote to extend the period to more than 15 days.

(c) Review At Next Meeting

If a Governor calls a membership proceeding for review within the time prescribed in paragraph (b), the NASD Board shall review the membership proceeding not later than the next meeting of the NASD Board. The NASD Board may order the Applicant and the Department to file briefs in connection with review proceedings pursuant to this paragraph.

(d) Decision of NASD Board, Including Remand

After review, the NASD Board may affirm, modify, or reverse the proposed written decision of the National Adjudicatory Council. Alternatively, the NASD Board may remand the membership proceeding with instructions. The NASD Board shall prepare a written decision that includes all of the elements described in Rule 1015[(i)(2)] (j)(2).

(e) Issuance of Decision

The NASD Board shall serve its written decision on the Applicant within 15 days after the meeting at

which it conducted its review. The decision shall constitute the final action of the Association for purposes of SEC Rule 19d-3, unless the NASD Board remands the membership proceeding.

1017. [Removal or Modification of Business Restriction] Application for Approval of Change in Ownership, Control, or Business Operations

(a) Events Requiring Application

[A member of the Association may seek modification or removal of a restriction on its business activities imposed pursuant to the Rule 1010 Series by filing a written application with the Department at the district office for the district in which the member's principal place of business is located. The application shall present facts showing that the circumstances that gave rise to the restriction have changed and state with specificity why the restriction should be modified or removed in light of the standards set forth in Rule 1014 and the articulated rationale for the imposition of the restriction. A copy of the decision and membership agreement pertaining to such restriction shall be appended to the application.]

A member shall file an application for approval of any of the following changes to its ownership, control, or business operations:

(1) a merger of the member with another member, unless both are members of the New York Stock Exchange, Inc. or the surviving entity will continue to be a member of the New York Stock Exchange, Inc.;

(2) a direct or indirect acquisition by the member of another member, unless the acquiring member is a member of the New York Stock Exchange, Inc.;

(3) a direct or indirect acquisition of substantially all of the member's assets, unless the acquirer is a member of the New York Stock Exchange, Inc.;

(4) a change in the equity ownership or partnership capital of the member that results in one person or entity directly or indirectly owning or controlling 25 percent or more of the equity or partnership capital; or

(5) a material change in business operations as defined in Rule 1011(i), unless the Department determines that an application is not required.

(b) Filing and Content of Application

(1) The member shall file the application with the Department at the district office in the district in which the member's principal place of business is located. If the application involves a merger between members with principal places of business in two or more districts, the application shall be filed and processed by the district office wherein the surviving firm's principal place of business will be located.

(2) The application shall describe in detail the change in ownership, control, or business operations and include a business plan, pro forma financials, an organizational chart, and written supervisory procedures reflecting the change.

(A) If the application requests approval of a change in ownership or control, the application also shall include the names of the new owners, their percentage of ownership, and the sources of their funding for the purchase and recapitalization of the member.

(B) If the application requests the removal or modification of a membership agreement restriction, the application also shall:

(i) present facts showing that the circumstances that gave rise to the restriction have changed; and

(ii) state with specificity why the restriction should be modified or removed in light of the standards set forth in Rule 1014 and the articulated rationale for the imposition of the restriction.

(C) If the application requests approval of an increase in Associated Persons involved in sales, offices, or markets made, the application shall set forth the increases in such areas during the preceding 12 months.

(c) Effecting Change and Imposition of Interim Restrictions

(1) A member shall file an application for approval of a change in ownership or control at least 30 days prior to such change. A member may effect a change in ownership or control prior to the conclusion of the proceeding, but the Department may place new interim restrictions on the member based on the standards in Rule 1014, pending final Department action.

(2) A member may file an application to remove or modify a membership agreement

restriction at any time. An existing restriction shall remain in effect during the pendency of the proceeding.

(3) A member may file an application for approval of a material change in business operations, other than the modification or removal of a restriction, at any time, but the member may not effect such change until the conclusion of the proceeding, unless the Department and the member otherwise agree.

(d) Rejection Of Application That Is Not Substantially Complete

If the Department determines within 30 days after the filing of an application that the application is not substantially complete, the Department may reject the application and deem it not to have been filed. In such case, within the 30 day period, the Department shall serve a written notice on the Applicant of the Department's determination and the reasons therefor. The Association shall refund the application fee, less $350, which shall be retained by the Association as a processing fee. If the Applicant determines to continue to apply for approval of a change in ownership, control, or business operations, the Applicant shall submit a new application and fee under this Rule.

[(b)] (e) Request for Additional Documents and Information

Within 30 days after the [receipt] filing of an application [to remove or modify a restriction], the Department shall [determine whether the application is complete, and if not, shall] serve a request for any additional information or documents necessary to render a decision [under paragraph (e)] on the application. The Department may serve subsequent requests for additional information or documents at any time during the application process. Unless otherwise agreed by the Department and the Applicant, the Applicant shall file any additional information and documents with the Department within 30 days after service of a request.

[(c) Lapse]

[(1) Absent a showing of good cause, an application to modify or remove a restriction shall lapse if an Applicant fails to:

(A) respond fully within 30 days after a request for information or documents;

(B) appear at or otherwise participate in a scheduled membership interview pursuant to paragraph (d); or

(C) return an executed membership agreement under paragraph (e)(4) within 25 days after service of the agreement.

(2) The lapse of an application shall require the Applicant to submit a new application to modify or remove a restriction under paragraph (a).]

[(d)] (f) Membership Interview

(1) The Department may require the Applicant to participate in a membership interview within 30 days after the [receipt] filing of the application, or if the Department requests additional information or documents, within 30 days after the filing of the additional information or documents by the Applicant.

(2) At least seven days before the membership interview, the Department shall serve on the Applicant a written notice that specifies the date and time of the interview and [the representative or representatives of the Applicant] persons who are required to participate in the interview. The Department shall serve the notice by facsimile or [commercial] overnight courier. The Applicant and the Department may agree to a shorter or longer period for notice or a different method of service.

(3) Unless the Department and the Applicant otherwise agree, the membership interview shall be conducted in the district office for the district in which the Applicant has its principal place of business.

(4) During the membership interview, the Department shall review the application and the considerations for the Department's decision set forth in paragraph [(e)(1)] (g)(1). The Department shall provide to the Applicant's representative or representatives any information or document that the Department has obtained from the Central Registration Depository or a source other than the Applicant and upon which the Department intends to base its decision under paragraph [(e)](g). If the Department receives such information or document after the membership interview or decides to base its decision on such information after the membership interview, the Department shall promptly serve the information or document and an explanation thereof on the Applicant.

[(e)] (g) Department Decision

(1) [In evaluating an application submitted under paragraph (a)] The Department shall consider

the application, the membership interview, other information and documents provided by the Applicant or obtained by the Department, the public interest, and the protection of investors.

(A) In rendering a decision on an application for approval of a change in ownership or control, or an application for approval of a material change in business operations that does not involve modification or removal of a membership agreement restriction, the Department shall determine if the Applicant would continue to meet the standards in Rule 1014(a) upon approval of the application.

(B) In rendering a decision on an application requesting the modification or removal of a membership agreement restriction, the Department shall consider whether maintenance of the restriction is appropriate in light of:

[(A)](i) the standards set forth in Rule 1014;

[(B)](ii) the circumstances that gave rise to the imposition of the restriction;

[(C)](iii) the Applicant's operations since the restriction was imposed;

[(D)] (iv) [a] any change in ownership or control or supervisors and principals; and

[(E)](v) any new evidence submitted in connection with the application.

(2) The Department shall [issue] serve a written decision on the application within 30 days after the conclusion of the membership interview or the [submission] filing of additional information or documents, whichever is later. If the Department does not require the Applicant to participate in a membership interview or request additional information or documents, the Department shall [issue] serve a written decision within 45 days after the [receipt] filing of the application under paragraph (a). The decision shall state whether the application [to modify or remove the restriction] is granted or denied in whole or in part, and shall provide a rationale for the Department's decision, referencing the applicable standard in Rule 1014.

(3) If the Department fails to [issue] serve a decision within 180 days after [receipt] filing of an application or such later date as the Department and the Applicant have agreed in writing, the Applicant may file a written request with the NASD Board requesting that the NASD Board direct the Department to issue a decision. Within seven days after [receipt] the filing of such a request, the NASD Board shall direct the Department to issue a written decision immediately or to show good cause for an extension of time. If the Department shows good cause for an extension of time, the NASD Board may extend the time limit for issuing a decision by not more than 30 days.

(4) If the Department [modifies or removes a restriction on the Applicant's business activities, the] approves an application under this Rule in whole or part, the Department may require an Applicant to file an executed membership agreement [submitted under Rule 1014 shall be modified accordingly].

[(f)](h) Service and Effectiveness of Decision

The Department shall serve its decision on the Applicant in accordance with Rule 1012. The decision shall become effective upon service and shall remain in effect during the pendency of any review until a decision constituting final action of the Association is [issued] served under Rule 1015 or 1016, unless otherwise directed by the National Adjudicatory Council, the NASD Board, or the Commission.

[(g)](i) Request for Review; Final Action

An Applicant may file a written request for review of the Department's decision with the National Adjudicatory Council pursuant to Rule 1015. The procedures set forth in Rule 1015 shall apply to such review, and the National Adjudicatory Council's decision shall be subject to discretionary review by the NASD Board pursuant to Rule 1016. If the Applicant does not file a request for a review, the Department's decision shall constitute final action by the Association.

[(h)](j) Removal or Modification of Restriction on Department's Initiative

The Department shall modify or remove a restriction on its own initiative if the Department determines such action is appropriate in light of the considerations set forth in paragraph [(e)(1)](g)(1). The Department shall notify the member in writing of the Department's determination and inform the member that it may apply for further modification or removal of a

restriction by filing an application under paragraph (a).

[1018. Change in Ownership, Control, or Operations]

[(a) Notice

At least 30 days prior to the occurrence of any of the following changes in ownership, control, or operations, a member shall file a written notice and application for continuance in membership with the Department at the district office in the district in which the member's principal place of business is located:

(1) a merger of the member with another member;

(2) an acquisition by the member of another member;

(3) an acquisition of substantially all of the member's assets;

(4) a change in the equity ownership or partnership capital of the member that results in one person or entity owning or controlling 25 percent or more of the equity or partnership capital; or

(5) a material change in the member's business operations.]

[(b) Review and Imposition of Interim Restrictions

The Department shall review a change in ownership, control, or operations described in paragraph (a) prior to the change taking effect. The Department may maintain existing restrictions on the member's business activities and place new interim restrictions on the member based on the standards in Rule 1014, pending final Department action.]

[(c) Request for Information

Within 30 days after receipt of the notice and application under paragraph (a), the Department shall request any additional information or documents necessary to render a decision under paragraph (f). Unless otherwise agreed by the Department and the Applicant, the Applicant shall file such additional information or documents with the Department within 30 days after the Department's request. The Department may request additional information and documents at any time during the application process; unless the Applicant and the Department agree otherwise, the Applicant shall file such information or documents within 30 days after the Department's request.]

[(d) Lapse

(1) Absent a showing of good cause, an application for continuance in membership shall lapse if an Applicant fails to:

(A) respond fully within 30 days after a request for information or documents;

(B) appear at or otherwise participate in a scheduled membership interview pursuant to paragraph (e); or

(C) return an executed membership agreement under paragraph (g) within 25 days after service of the agreement.

(2) The lapse of an application shall require the Applicant to submit a new application under paragraph (a).]

[(e) Membership Interview

(1) The Department may require the Applicant to participate in a membership interview. The membership interview shall be held within 30 days after the receipt of the application, or if the Department requests additional information or documents, within 30 days after the filing of such additional information or documents by the Applicant.

(2) At least seven days before the membership interview, the Department shall serve on the Applicant a written notice that specifies the date and time of the interview and the representative or representatives of the Applicant who are required to participate in the interview. The Department shall serve the notice by facsimile or commercial courier. The Applicant and the Department may agree to a shorter or longer period for notice or a different method of service.

(3) Unless the Department and the Applicant otherwise agree, the membership interview shall be conducted in the district office for the district in which the Applicant has or intends to have its principal place of business.

(4) During the membership interview, the Department shall review the application and the considerations for the Department's decision set forth in paragraph (f). The Department shall provide to the Applicant's representative or representatives any information or document that the Department has obtained from the Central Registration Depository or a source other than the Applicant and upon which the Department intends to base its decision under paragraph (f). If the Department receives such information or document after the membership interview or decides to base its decision on such information after the membership interview,

the Department shall promptly serve the information or document and an explanation thereof on the Applicant.]

[(f) Department Decision

(1) In evaluating an application submitted under paragraph (a), the Department shall consider whether the Applicant continues to meet the standards set forth in Rule 1014 in light of the change in ownership, control, or operations, and whether current restrictions, if any, or new restrictions are necessary for the Applicant to continue to meet such standards.

(2) The Department shall issue a written decision within 30 days after the membership interview or the submission of additional information or documents, whichever is later. If the Department does not require the Applicant to participate in a membership interview or submit additional information or documents, the Department shall issue a written decision within 45 days after receipt of an application under paragraph (a). The decision shall state the terms for continuance in NASD membership, whether current restrictions, if any, are maintained or new restrictions are imposed, and shall provide a rationale for the Department's decision, referencing the applicable standard in Rule 1014.

(3) If the Department fails to issue a decision within 180 days after receipt of an application or such later date as the Department and the Applicant have agreed in writing, the Applicant may file a written request with the NASD Board requesting that the NASD Board direct the Department to issue a decision. Within seven days after receipt of such a request, the NASD Board shall direct the Department to issue a written decision immediately or to show good cause for an extension of time. If the Department shows good cause for an extension of time, the NASD Board may extend the time limit for issuing a decision by not more than 30 days.]

[(g) Submission of Membership Agreement

The Department may condition approval of an application for continuance in membership on the Applicant's submission of a new written membership agreement pursuant to Rule 1014(c).]

[(h) Service and Effectiveness of Decision

The Department shall serve its decision on the Applicant in accordance with Rule 1012. The decision shall become effective upon service and shall remain in effect during the pendency of any review until a decision constituting final action of the Association is issued under Rule 1015 or 1016, unless otherwise directed by the National Adjudicatory Council, the NASD Board, or the Commission.]

[(i) Request for Review; Final Action

An Applicant may file a written request for review of the Department's decision with the National Adjudicatory Council pursuant to Rule 1015. The procedures set forth in Rule 1015 shall apply to such a review, and the National Adjudicatory Council's decision shall be subject to discretionary review by the NASD Board pursuant to Rule 1016. If the Applicant does not file a request for review, the Department's action shall constitute the final action of the Association.]

1018. Stay of Application During Pendency of Criminal or Other Proceeding

(a) The Department may stay an application filed under Rule 1013 or 1017 if:

(1) a state or federal authority files criminal charges against the Applicant or a principal or proposed principal of the Applicant;

(2) the Commission files a complaint or a request for injunctive relief against the Applicant or a principal or proposed principal of the Applicant; or

(3) the Association, another self-regulatory organization, or a state files a disciplinary complaint against the Applicant or a principal or proposed principal of an Applicant alleging a violation of a law or rule listed in IM-1011-1 (or a comparable state law, rule, or regulation).

In such case, the application shall be stayed during the pendency of the proceeding. If the Department has imposed interim restrictions under Rule 1017(c), the restrictions shall remain in effect during the stay.

(b) If the Applicant or principal or proposed principal prevails in the proceeding, the stay shall be lifted automatically.

(c) If there is a material change in the circumstances that gave rise to the stay, the Applicant may file a written request with the Department to lift the stay. The Department shall serve a written response on the Applicant within 14 days after

the filing of the request by the Applicant. If the Department denies the request, the Applicant may file a written request for review with the National Adjudicatory Council. The National Adjudicatory Council or the Review Subcommittee shall serve a written response on the Applicant within 30 days.

1019. Application to Commission for Review

A person aggrieved by final action of the Association under the Rule 1010 Series may apply for review by the Commission pursuant to Section 19(d)(2) of the Act. The filing of an application for review shall not stay the effectiveness of a decision constituting final action of the Association, unless the Commission otherwise orders.

Attachment B

Rule 1011
Associated Person

The definition of "Associated Person" is amended to clarify that it includes only natural persons.

Material Change In Business Operations

The term "material change in business operations" is defined for the first time. The definition is significant because it triggers a requirement for a member to apply to the district office for approval of the change under proposed Rule 1017.

NASD Regulation does not believe that it is possible to develop an exhaustive definition of the term "material change in business operations." If a change in a member's business falls outside of the definition, or the safe harbor described below (*e.g.*, because it exceeded the safe harbor limits or the member has disciplinary history), then the member may contact the district office to determine if the district would deem the change to be material. A member is not required to contact the district office if the member believes the change is not material. Nonetheless, the staff ultimately has the authority to determine whether a change not specified in the definition is material. If the staff determines that a change is indeed material after it is made, then the member potentially could be subject to disciplinary action for failure to file an application under proposed Rule 1017.

Safe Harbor Limits

Proposed Interpretive Material 1011-1 (IM-1011-1) is added to create a safe harbor for certain changes that are presumed not to be material and therefore do **not** require a member to submit an application for approval of the change. NASD Regulation requests comment on whether the limitations in the Interpretive Material are set at appropriate levels.

The safe harbor would not be available to members that have "disciplinary history." "Disciplinary history" means a finding of a violation in the past five years by the SEC, a self-regulatory organization, or a foreign financial regulatory authority of one or more of the following provisions (or comparable foreign provisions):

- Section 15(b)(4)(E) of the Securities Exchange Act of 1934 (failure to supervise);
- Section 17(a) of the Securities Act of 1933 (fraudulent interstate transactions);
- SEC Rules—
  - 10b-5 (fraud and manipulation), and
  - 15g-1 through 15g-9 (penny stock rules);
- NASD Rules—
  - 2110 (just and equitable principles of trade),
  - 2120 (fraud and manipulation),
  - 2310 (suitability),
  - 2330 (protection of customer securities and funds),
  - 2440 (fair prices and commissions),
  - 3010 (failure to supervise requirements only),
  - 3310 (manipulative and deceptive quotations), and
  - 3330 (payments to influence market prices); and
- MSRB Rules—
  - G-19 (suitability),
  - G-30 (prices and commissions), and
  - G-37(b) & (c) (political contributions).

NASD Regulation requests comment on whether this definition is appropriate, particularly the five-year limit. NASD Regulation also requests comment on whether the definition of disciplinary history should include violations by officers or principals of the member.

Principal Place Of Business

The term "principal place of business" is defined for the first time. An applicant's principal place of business determines which district office will process its application. "Principal place of business" means the location where the officers, partners, or managers direct and control the activities of the applicant, unless NASD Regulation staff designates a different location. That location may be where the largest number of associated persons are located or where the books and records are kept. This definition is designed to prevent an applicant from trying to select a particular district office to process its application through its designation of a principal place of business.

Sales Practice Event

NASD Regulation proposes to redefine "sales practice violations" as "sales practice event" because the definition includes not only proven violations, but also unproven allegations. The current definition has become obsolete; it tracks a definition that was once used on Form U-4. The proposed definition includes any customer

complaint, arbitration, or civil litigation that has been or is required to be reported to the Central Registration Depository (CRD℠) or otherwise is required to be reported to the Association (*e.g.*, via Rule 3070).

Rule 1012

NASD Regulation proposes to amend the service and filing provisions to permit additional methods of delivery and to use consistent terminology for calculating deadlines. The term "commercial courier" is replaced with "overnight courier" to clarify that applicants and NASD Regulation staff may use the overnight delivery service offered by the United States Postal Service. NASD Regulation intends the term "overnight courier" to refer to any entity that regularly provides such overnight delivery services, such as Federal Express, DHL, or the United States Postal Service. Use of the term "overnight courier" is not intended to imply that only actual overnight delivery may be used under the Rule. Overnight delivery should be used if it is available. However, if overnight delivery is not available for a particular location, the applicant or NASD Regulation staff may use the most rapid delivery option available (*e.g.*, two day service) from the overnight courier and still be in compliance with the Rule.

The lapse of application provisions are consolidated and moved from Rules 1013(b), 1017(c), and 1018(d) to proposed Rule 1012(b) for ease of reference. The lapse rule, which is discussed in greater detail in the next section, permits the staff to discontinue processing an application if an applicant does not timely provide requested information or documents. The only changes to the lapse rule are to:

- permit the staff and the Applicant to agree on a submission date for the membership agreement, rather than requiring that all agreements be submitted within 25 days, and
- clarify that fees are not refunded for lapsed applications.

Rule 1013

One of the major changes to this Rule is to simplify application submission procedures. Currently, this Rule requires applicants to submit their applications in two parts. Part One, which includes primarily forms and fees (*e.g.*, the Forms BD and U-4), is sent directly to CRD in Rockville, Maryland, for processing. Part Two, which includes all remaining documents required for member admission, is sent to the district office that will review the application. At the time the rule was adopted, the staff thought it would be more efficient to send each part to the location where it would be processed. In practice, this has created problems when both parts of the application are not submitted at the same time, or one or both parts are incomplete, making it difficult to determine when the application should be treated as filed and when the staff should begin reviewing it. The application filing date is critical because the 180-day limitation placed on the staff for rendering a decision on the application is measured from this date.

To alleviate these problems, NASD Regulation recommends one point of entry for the entire application - the district office. District staff will review the entire application to determine if it is substantially complete. If so, they will forward any documents that need to go to CRD and continue processing the application.

NASD Regulation proposes a new rule for dealing with applications that are not substantially complete at the time of submission. Currently, the staff does not have any authority to refuse to begin processing an inadequately prepared application. Instead, they attempt to begin processing such an application by sending a request for further information to the applicant. If the applicant does not timely provide the requested information, then the rules permit the staff to "lapse" the application. The staff then notifies the applicant that the application has lapsed, all fees are forfeited, and the applicant is required to start over with the application process if it still wants to become an NASD member. These procedures can consume as much as 90 days and a considerable amount of staff and applicant resources, but still result in a rejected application.

Under the proposed rule, if an application is so deficient upon initial submission that the staff cannot begin processing it (*e.g.*, it is missing major components of the application, such as written supervisory procedures or a business plan), then the staff may reject the application. The staff would have no more than 30 days after submission to do this, and would be required to provide reasons for its action in writing. NASD Regulation proposes a $350 processing fee for the rejection of an application that is not substantially complete.[2] NASD Regulation considered but rejected defining the term "substantially complete" because the determination will vary depending on the type and complexity of the proposed business, among other things. The lapse rules will still apply to those situations where an applicant stops providing information in the middle of the application process.

Rule 1013 also is simplified by

removing requirements for applicants to submit information that has already been submitted to CRD. The district staff has full access to CRD and can obtain the information they need directly from it. This change will make the application process simpler for applicants by eliminating duplicative submissions to NASD Regulation.

The proposed rule adds new requirements for applicants to submit information concerning their ability to ensure business continuity, including information about the capacity of their communications and operational systems, contingency plans, disaster recovery plans, and the like. NASD Regulation also proposes a new standard for admission that requires that such systems, plans, and procedures be adequate. The staff would not be required to investigate the adequacy themselves; rather, the applicant would certify that the systems, plans, and procedures are adequate for the applicant's business. The applicant may rely on a third party (*e.g.*, a vendor of such a system) to provide the certification if the applicant so chooses. NASD Regulation requests comment on what sort of certification would be appropriate, who may prepare it, and what it should contain.

NASD Regulation also wishes to clarify that under Rule 1013(b)(4), the applicant and the staff may agree to hold the membership interview at the applicant's place of business.

Rule 1013 is amended by adding new subparagraph (b)(5) to require applicants to provide updated financial information at the time of their membership interview.

Rule 1014

NASD Regulation proposes few changes with respect to the standards for admission. NASD Regulation proposes a new standard with respect to business continuity, as described above. NASD Regulation also proposes that the applicant's supervisory procedures specifically must include procedures to ensure proper registrations are obtained by the firm. All other changes to the standards for admission are conforming changes.

NASD Regulation also considered the requirement of Rule 1014(a)(9)(C) that prospective supervisors have at least one year of direct experience or at least two years of related experience in the subject area to be supervised. NASD Regulation believes that this requirement should continue to be imposed and has published interpretive guidance on this subject in *How To Become A Member*, which is available online at *www.nasdr.com/4700_appendix_b.htm*. NASD Regulation does not believe that supervisory experience requirements should be increased.

Rule 1014(c), which concerns the submission of membership agreements, is amended by deleting the requirement that any member with a membership agreement obtain approval from NASD Regulation of any change in business outside the terms of the agreement. NASD Regulation believes that this provision is too restrictive, particularly for firms with no disciplinary history. The provision also puts members with a membership agreement at a disadvantage vis-à-vis members that do not have a membership agreement.[3] Therefore, this provision is deleted.

When the proposed rules become effective, to ensure that members are treated equally, NASD Regulation will permit members that are eligible for the safe harbor to use it, even if their membership agreement includes a requirement to obtain approval from NASD Regulation of any change in business outside the terms of the agreement. When NASD Regulation examines a member, it will update the membership agreement to reflect the new rule.

NASD Regulation also requests comment on whether restrictions in a membership agreement should automatically sunset after a fixed period (*e.g.*, five years) if the applicant does not have any disciplinary history.

In addition, upon adoption of the proposed rules, NASD Regulation will begin including business expansion plans in membership agreements to the extent practicable.

Rule 1015

NASD Regulation proposes to delete the NAC's call for review authority. Under current Rule 1015, the NAC or the Review Subcommittee may call for review a district decision on a membership application, even if the applicant does not appeal the decision. NASD Regulation considered at length whether a procedure or policy could be developed to implement this provision effectively, but ultimately determined that it is unworkable.

Member admission decisions do not lend themselves to calls for review. This is especially true for decisions that grant a membership application without restriction because they do not contain a rationale. (Only decisions that deny an application or grant it with a restriction contain a rationale. Decisions that grant an application without restriction simply state that the applicant has met all relevant standards.) Just reading the districts' decisions, without looking at the rest of the record, would not

be particularly useful. Unlike a call for review of a regular disciplinary decision, there is no hearing panel vote that might indicate a close or difficult issue. NASD Regulation believes that it would be duplicative of district staff work and inefficient to review every record in its entirety to determine if it supports the decision. NASD Regulation also considered whether certain categories of decisions could be reviewed, but was concerned that such a procedure might be perceived as biased against those firms that fell within the selected category.

Therefore, NASD Regulation has temporarily suspended calls for review of membership decisions, and proposes to delete this provision altogether. NASD Regulation headquarters staff will continue to exercise oversight of the district decision-making process.

NASD Regulation also proposes a new provision for dismissing appeals that are abandoned by an applicant.

Rule 1017

Current Rule 1017, which addresses applications for removal or modification of a business restriction, and Rule 1018, which addresses applications for approval of changes in ownership, control, or operations, are consolidated in proposed Rule 1017. Sometimes a member initiates business changes that involve both rules, which creates confusion as to which rule should be used. Therefore, NASD Regulation proposes to consolidate these rules to make them easier for staff and applicants to use and to eliminate any confusion that may arise from overlapping provisions.

This consolidation is achieved in part by defining the term "material change in business operations" in proposed Rule 1011(i) to include the removal or modification of a business restriction. All material changes in business operations would trigger a review under proposed Rule 1017.

Members should note that a "restriction" is specifically labeled as such in the membership agreement, and NASD Regulation issues a decision that states the rationale for the restriction. A restriction is distinct from other limitations that a member may set forth in its business plan that may be recited as part of the "Business Activities" section of a membership agreement.

For example, an applicant may indicate in its business plan that it intends to have 10 to 20 registered representatives and make markets in no more than 10 stocks. If the NASD approves the application, these self-imposed limitations, which have been considered as part of the application, may be included in the "Business Activities" section of the membership agreement. These types of limitations are not considered "restrictions" under the Rules because they are not imposed by NASD Regulation, and therefore NASD Regulation does not have to include a rationale for them in the decision in the application. Under the proposed Rules, a member that has such limitations in its membership agreement may expand beyond those limitations without prior review and approval by NASD Regulation to the extent permitted in the safe harbor in IM-1011-1.

Another type of change that triggers an application under proposed Rule 1017 is a direct or indirect change in the ownership or control of the member. NASD Regulation wishes to clarify that a group of individuals acting in concert to obtain control of 25 percent or more of the equity or partnership capital of a member will be deemed to be an "entity" under the Rule, and as such, trigger the requirement to submit an application to obtain approval of the ownership/control change.

NASD Regulation proposes to discontinue its review of certain ownership or control changes. Under proposed Rule 1017, NASD Regulation would discontinue review of member mergers and acquisitions that are reviewed by the New York Stock Exchange, thereby eliminating duplication by self-regulatory organizations.

Proposed Rule 1017 also sets forth for the first time what type of information should be included in an application and the content of the staff's decision on an application under this rule. The Rule also clarifies when the application should be filed and what changes can be effected prior to obtaining NASD Regulation's approval.

NASD Regulation requests comment on whether a new provision should be added to proposed Rule 1017 to clarify what happens if a change in ownership is denied. For example, the Rule could provide that if the ownership change is denied, then the member cannot engage in the securities or investment banking business, and that the firm has a fixed period of time to find new owners or file a Form BDW. Of course, as under the current rules, a member could continue to operate with the approved owners if the transaction has not closed or otherwise could be unwound.

As part of its review of the Rule 1010 Series, NASD Regulation considered whether the time frames in proposed Rule 1017 could be shortened so that the overall process would be completed in 90 days. NASD Regulation determined

not to shorten the time frames at this time because other rule revisions (*e.g.*, defining material change in operations and listing the documents required for the application) should speed up processing of applications. NASD Regulation is working on additional guidance to members on what types of documents and information the staff will require if a member requests approval to engage in certain specialized areas of the securities or investment banking business. This guidance will be posted on the Web Site in the future. NASD Regulation believes that these changes should be given a chance to work before any time frames are shortened. NASD Regulation will reconsider the issue one year after the rule revisions have become effective and more information is available about the processing time for applications.

Rule 1018

NASD Regulation proposes to adopt a new Rule 1018, which would permit the staff to stay a membership application under Rule 1013 or 1017 if:

- a state or federal authority files criminal charges against the applicant or a principal or proposed principal of the applicant;
- the SEC files a complaint or a request for injunctive relief against the applicant or a principal or proposed principal of the applicant; or
- the NASD, another self-regulatory organization, or a state files a complaint alleging a violation of one of the laws or rules listed in proposed IM-1011-1 (or a comparable state provision).

Under the proposed rule, the stay would be lifted automatically if the applicant prevailed in the disciplinary action. The staff also would be authorized to lift the stay if circumstances changed. If the staff denied the request to lift the stay, the applicant could appeal to the National Adjudicatory Council.

Summary of Requests for Specific Comments

NASD Regulation encourages members and other interested parties to comment on all aspects of the proposed rules discussed in this *Notice*. We also specifically solicit comment on the following issues:

- the definition of material changes in business operations in proposed Rule 1011(i);
- the safe harbor numbers set forth in proposed IM-1011-1;
- the definition of disciplinary history in proposed IM-1011-1;
- whether the definition of disciplinary history should include violations by officers or principals of the member;
- how an applicant should demonstrate that it can ensure business continuity under proposed Rule 1014(a)(6);
- whether restrictions in a membership agreement should automatically sunset after a fixed period (*e.g.*, five years) if the applicant does not have any disciplinary history; and
- whether a provision should be added to proposed Rule 1017 that clarifies what happens if a change in ownership is denied, *e.g.*, whether the Rule specifically should provide that if the ownership change is denied, then the member cannot engage in the securities or investment banking business, and that the firm has a fixed period of time to find new owners or file a Form BDW.

Endnotes

[1]Members of the Committee are: Faith Colish, New York, New York; Linda Lerner, All-Tech Investment Group, Inc., Montvale, New Jersey; Brian T. Shea, Pershing, Jersey City, New Jersey; Theodore W. Urban, Ferris, Baker Watts, Incorporated, Washington, D.C.; and Richard P. Woltman, Spelman & Co., Inc., San Diego, California. Mr. Urban chairs the Committee.

[2]NASD Regulation also proposes to charge a $350 processing fee for Rule 1017 applications that are not substantially complete. Currently, NASD Regulation does not charge a fee for Rule 1017 applications, but anticipates doing so in the future.

[3]In 1984, the SEC approved a codification of the NASD's member admission procedures, which included a requirement that any restriction on a member's business be included in a membership agreement executed by the member. See Exchange Act. Rel. No. 21159, 49 FR 30268 (Jul. 27. 1984) (File No. SR-NASD-82-24). Thus, a member admitted before 1984 or a member admitted without any restriction from 1984 to 1997 may not have a membership agreement. In 1997, NASD Regulation began requiring all new members to execute a membership agreement, regardless of whether NASD Regulation imposed any restriction. See NASD Rule 1014(c); Exchange Act Rel. No. 38908 (Aug. 7, 1997); 62 FR 43385 (Aug. 13, 1997) (File No. SR-NASD-97-28).

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NASD Notice to Members 99-68

NASD Regulation Announces Its Policy On Enforcement Of Disciplinary Sanctions During The Pendency Of Circuit Court Appeals

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Executive Summary

NASD Regulation, Inc. (NASD Regulation®) announces its policy to refrain from enforcing disciplinary sanctions, other than bars and expulsions, during the pendency of appeals of National Association of Securities Dealers, Inc. (NASD®) disciplinary cases from the Securities and Exchange Commission (SEC) to Circuit Courts of Appeal.

Questions regarding this *Notice to Members* may be directed to Carla Carloni, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8019.

Discussion

In accordance with long-standing practice, NASD Regulation does not bill respondents for disciplinary fines during the course of Circuit Court appeals, notwithstanding whether sanctions are stayed in the matter. In the past, however, NASD Regulation enforced suspensions in cases in which sanctions were not stayed pending Circuit Court appeals. Thus, while NASD Regulation refrained from billing respondents for fines imposed in NASD disciplinary cases pending appeal to Circuit Courts of Appeal, it imposed suspensions and requalification requirements in the very same cases.

In order to harmonize NASD Regulation's sanction enforcement efforts in cases pending appeal to Circuit Courts of Appeal, NASD Regulation has revisited its policy and concluded that the most efficient and fairest method of dealing with the enforcement of sanctions at the Court of Appeals level (and during the pendency of petitions for certiorari or ongoing proceedings before the U.S. Supreme Court) is to follow the policy that it currently follows at the SEC appellate level, *i.e.*, enforce only bars and expulsions (absent a stay), but refrain from enforcing all other sanctions, regardless of whether a stay is in effect. This method ensures investor protection by enforcing bars and expulsions while fairly providing respondents with the opportunity to pursue appeals without the threat of the enforcement of other sanctions.

Legally, NASD Regulation can enforce sanctions absent a stay while a matter is pending appeal in a Circuit Court of Appeals. NASD Regulation has concluded, however, that the fairer and more efficient policy is to refrain from doing so for the following reasons:

1) If a Court of Appeals reverses SEC/NASD findings, the sanctions may be eliminated. If an individual or a firm is forced to serve a suspension or to requalify while an appeal is pending, he/she will have done so for naught if the sanction ultimately is eliminated. NASD cannot return suspension time to an individual or a member firm if the findings are reversed, so the individual or firm loses that time in the industry.

2) Consistency is important in the area of enforcement of sanctions. Since NASD Regulation refrains from collecting fines and revoking respondents for failing to pay fines while an appeal is pending in a Circuit Court of Appeals, it is inconsistent to require that those same respondents serve suspensions while a matter is pending appeal.

3) An across-the-board policy to refrain from enforcing all sanctions (except bars and expulsions) while cases are on appeal will ensure that NASD Regulation does not inadvertently violate a stay

order. Although ideally NASD Regulation receives timely notice of all stay orders, since it is not always noticed as a party to Circuit Court appeals, there is a danger that timely notice may not be forthcoming.

4) The SEC readily grants stay requests when matters are pending appeal in a Circuit Court of Appeals. In many cases, a stay already is in effect, so this policy change should not drastically alter the current state of affairs with respect to the enforcement of sanctions.

5) Since NASD Regulation always enforces bars and expulsions (absent a stay), the investing public is protected in cases involving more egregious misconduct.

NASD Regulation believes that this policy change will ensure the fair and efficient treatment of all disciplinary respondents with respect to the enforcement of sanctions pending Circuit Court appeals.

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NASD Notice to Members 99-69

NASD Regulation Requests Comment On Proposed Trading Halt Rules; Comment Period Expires **September 30, 1999**

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- ☐ Systems
- ■ Trading
- ■ Training
- ☐ Variable Contracts

Executive Summary

As part of the effort to address abuses in the trading and sales of thinly traded, thinly capitalized (microcap) securities and to increase investor protection in the trading of over-the-counter (OTC) securities, this *Notice* requests comment on a rule proposal that would authorize NASD Regulation, Inc. (NASD Regulation®) to halt quotations and trading in OTC securities under certain circumstances. For purposes of this rule, OTC securities include securities that are not listed on an exchange or on The Nasdaq Stock Market, Inc. (Nasdaq®) and securities that are not quoted on the OTC Bulletin Board® (OTCBB).

Under the proposed rule, NASD Regulation would be authorized to impose halts:

> (1) in conjunction with regulatory trading halts imposed by foreign regulatory authorities because of potential fraudulent conduct; and
>
> (2) when the security is a derivative of a security listed on Nasdaq or on a national securities exchange and Nasdaq or an exchange halts trading in the underlying security.

Nasdaq has filed a rule proposal with the Securities and Exchange Commission (SEC) requesting authorization for similar authority with regard to OTCBB securities.

Request For Comment

NASD Regulation encourages all interested parties to comment on the proposal. Comments must be received by **September 30, 1999**. Comments should be mailed to:

Joan Conley
Office of the Corporate Secretary
NASD Regulation, Inc.
1735 K Street, NW
Washington, D.C. 20006-1500

or e-mailed to:
pubcom@nasd.com

***Important Note*:** The only comments that will be considered are those submitted via e-mail or in writing.

Before becoming effective, any rule change developed as a result of comments received must be adopted by the NASD Regulation Board of Directors, may be reviewed by the National Association of Securities Dealers, Inc. (NASD®) Board of Governors, and must be approved by the SEC.

Questions/Further Information

As noted, written comments should be submitted to Joan Conley. Questions concerning this *Notice to Members—Request for Comment* may be directed to Mary Revell, Associate General Counsel, NASD Regulation, at (202) 728-8203.

Foreign Regulatory Authority Trading Halts

Currently, NASD rules do not provide for the implementation of trading or quotation halts in any security that is not listed on an exchange or on Nasdaq. Thus, NASD Regulation and Nasdaq are unable to impose trading halts in securities that are quoted on the OTCBB (OTCBB securities) or in securities that are quoted and traded in other quotation media, such as the National Quotation Bureau's Pink Sheets or Instinet (OTC securities).

This *Notice* solicits comment on whether NASD Regulation should have the authority to impose regulatory trading and quotation halts in OTC securities, in conjunction with certain halts imposed by a foreign securities exchange, market, or regulatory authority overseeing the foreign market (foreign regulatory authority). The proposed rule would apply only to OTC securities that are not included in the OTCBB and are not listed on a national securities exchange or Nasdaq.[1]

Foreign regulatory authorities impose trading halts for various reasons, depending on the jurisdiction, including the dissemination of material news, an issuer's failure to meet regulatory filing requirements imposed by a foreign market or regulatory authority, operational reasons (*e.g.*, an order imbalance), and public interest reasons. The proposed rule would authorize NASD Regulation to impose trading and quotation halts in OTC securities in conjunction with a foreign regulatory authority halt that is imposed because of potential fraudulent conduct or other public interest concerns, when this is stated in the foreign trading halt order. NASD Regulation would not impose a halt in conjunction with a foreign regulatory authority trading halt that is imposed solely for late filings, the dissemination of material news, or operational reasons.[2] The halt would be imposed for a maximum of five trading days. At that time, Market Makers would be required to fulfill their obligations under SEC Rule 15c2-11 prior to initiating either a priced or unpriced quotation in the security.[3]

NASD Regulation would notify the trading community and the public of the halt through the NASD Regulation and Nasdaq Trader Web Sites (*www.nasdr.com* and *www.nasdaqtrader.com*) and upon issuance of the notice will prohibit quotations in any quotation medium and trading by any NASD member. The trading halt notice (noting the beginning and end dates) would remain on the Web Sites for a period of time to inform the public and the trading community of the halt, and ensure ongoing compliance with Rule 15c2-11.[4]

Derivative Security Trading Halts

NASD Rule 4120 provides Nasdaq with the authority to halt trading in a derivative security, in conjunction with a halt imposed by Nasdaq or a national securities exchange in the underlying equity security, but only if the derivative is listed on Nasdaq. Thus, when Nasdaq or an exchange halts trading in a listed security, trading is allowed to continue in the underlying unlisted derivatives on the OTCBB and in other OTC quotation media. It is difficult to accurately price the derivative in the absence of current price information for the underlying security. This difficulty in pricing may lead to disorderly markets and investor confusion.

This *Notice* solicits comment on whether NASD Regulation should have the authority to halt trading in OTC derivatives in conjunction with a trading halt imposed by Nasdaq or an exchange in the underlying listed security. Like the provision described above, this rule will apply only to OTC securities that are not included in the OTCBB and are not listed on a national securities exchange or Nasdaq.[5]

Plan of Allocation and Delegation of Functions

Finally, NASD Regulation proposes to amend the Plan of Allocation and Delegation of Functions to clarify that the Stockwatch section of Nasdaq would have the authority to handle trading halt functions for securities traded in the OTC market.

Text of Proposed Rule

(Note: New text is underlined; deletions are in brackets.)

Rule 3900. Trading and Quotation Halts in Non-Nasdaq, Non-OTCBB Over-the-Counter Securities

(a) Authority to Initiate Trading and Quotation Halts

In circumstances in which it is necessary to protect investors and the public interest, NASD Regulation may direct members, pursuant to the procedures set forth in paragraph (b), to halt trading and quotations in the over-the-counter ("OTC") market of an American Depository Receipt ("OTC ADR") or a security ("OTC Security") that is traded in the OTC market and that is not otherwise listed on The Nasdaq Stock Market ("Nasdaq") or a national securities exchange or included in the OTCBB when:

(1) the OTC Security or the security underlying the OTC ADR is listed on or registered with a foreign securities

exchange or market, and the foreign securities exchange, market, or regulatory authority overseeing such issuer, exchange or market, halts trading in such security for regulatory reasons ("Foreign Regulatory Halt"); provided, however, that NASD Regulation will not impose a trading and quotation halt if the Foreign Regulatory Halt was imposed solely for the dissemination of material news, a regulatory filing deficiency, or operational reasons; or

(2) the OTC Security is a derivative or component of a security listed on a national securities exchange or Nasdaq ("listed security") and a national securities exchange or Nasdaq imposes a trading halt in the listed security.

(b) Procedure for Initiating a Trading and Quotation Halt

(1) For a halt initiated under subparagraph (a)(1) of this rule, NASD Regulation will promptly evaluate information received from a foreign securities exchange or market on which the OTC Security or the security underlying the OTC ADR is listed or registered or from a foreign regulatory authority overseeing such issuer, exchange, or market about a Foreign Regulatory Halt and determine whether a trading and quotation halt in the OTC Security is appropriate.

(2) For a halt initiated under subparagraph (a)(2) of this rule, NASD Regulation will promptly evaluate information received from Nasdaq or a national securities exchange about a trading halt imposed in a listed security and determine whether a trading and quotation halt in the OTC Security is appropriate.

(3) Should NASD Regulation determine that a basis exists under this Rule for initiating a trading and quotation halt, NASD Regulation shall disseminate appropriate public notice that a trading and quotation halt is in effect and the commencement of the trading and quotation halt will be effective simultaneous with appropriate public notice.

(4) Trading and quotations in the OTC market may resume when NASD Regulation determines that the basis for the halt no longer exists or when five business days have elapsed from the date NASD Regulation initiated the trading and quotation halt in the security, whichever occurs first. NASD Regulation shall disseminate appropriate public notice that a trading and quotation halt is no longer in effect.

(c) Violation of OTC Trading and Quotation Halt Rule

If a security is subject to a trading and quotation halt initiated pursuant to this rule, it shall be deemed conduct inconsistent with just and equitable principles of trade and a violation of Rule 2110 for a member:

(i) to effect, directly or indirectly, a trade in such security; or

(ii) publish a quotation, a priced bid and/or offer, an unpriced indication of interest (including "bid wanted" and "offer wanted" indications), or a bid or offer accompanied by a modifier to reflect unsolicited customer interest, in any "quotation medium." For purposes of this Rule, "quotation medium" shall mean any quotation system, publication, electronic communication network, or any other device, including any issuer or inter-dealer quotation system, that is used to regularly disseminate quotations or indications of interest in transactions in equity securities.

Plan Of Allocation And Delegation Of Functions By NASD To Subsidiaries

I - III. No Change

IV. Stockwatch

The Stockwatch section handles the trading halt functions for The Nasdaq Stock Market *securities*, exchange-listed securities traded in the over-the-counter market (i.e., the Third Market), *securities quoted in the Over-the-Counter Bulletin Board* [.] , and all other securities traded in the over-the-counter market.[6] Review of all questionable market activity, possible rule infractions or any other matters that require any type of investigative or regulatory follow-up will be referred to and conducted by NASD Regulation, which will assume sole responsibility for the matter until resolution. This responsibility will include examinations, investigations, document requests, and any enforcement actions that NASD Regulation may deem necessary. NASD Regulation staff at all times will have access to all records and files of the Stockwatch function.

Endnotes

[1]Nasdaq has filed a proposed rule change with the SEC seeking similar authority with respect to OTCBB securities. File No. SR-NASD-99-33, submitted to the SEC on July 13, 1999. NASD Rule 4120 already provides Nasdaq with the authority to halt trading of Nasdaq-listed securities and exchange-listed securities traded OTC.

[2]NASD Regulation and Nasdaq do not propose to halt for the dissemination of material news because Nasdaq does not have any

listing agreement with OTC issuers and thus cannot compel the full disclosure and dissemination of material news. NASD Regulation and Nasdaq do not propose to halt trading if an issuer fails to meet filing requirements imposed by a foreign regulatory authority on OTC issuers when such requirements may not currently exist in the United States for such issuers. Finally, NASD Regulation and Nasdaq are not proposing to halt trading based on a foreign exchange's operational halt, such as for an order imbalance, because Nasdaq does not generally halt trading for operational reasons.

[3]SEC Rule 15c2-11, with certain exemptions, prohibits a broker/dealer from publishing a quotation for an OTC security in any quotation medium unless the broker/dealer reviews the information specified in the Rule regarding the security and its issuer and has a reasonable belief that the information is accurate and from a reliable source. NASD Rule 6740 requires a broker/dealer to make a filing on Form 211 with the NASD demonstrating compliance with SEC Rule 15c2-11 prior to publishing a quotation for an OTC security.

[4]When informed, NASD Regulation would also publish notice of foreign regulatory halts imposed for late regulatory filings on the Web Sites even though NASD Regulation will not impose a simultaneous trading halt. NASD Regulation will not provide notice or impose a trading halt if a foreign regulatory authority halts trading for the dissemination of material news or for operational reasons (*e.g.*, an order imbalance).

[5]The proposed rule change described in footnote 1 also seeks authority for Nasdaq to halt trading in OTCBB derivatives.

[6]Italics indicate language proposed to be added in rule filing described in footnote 1.

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NASD Notice to Members 99-70

NASD Regulation Announces New Web-Based FOCUS Filing System—To Be Available For September 1999 Filings

Suggested Routing

- ■ Senior Management
- ☐ Advertising
- ☐ Continuing Education
- ☐ Corporate Finance
- ■ Executive Representatives
- ☐ Government Securities
- ☐ Institutional
- ☐ Insurance
- ☐ Internal Audit
- ■ Legal & Compliance
- ☐ Municipal
- ☐ Mutual Fund
- ■ Operations
- ☐ Options
- ☐ Registered Representatives
- ☐ Registration
- ☐ Research
- ☐ Syndicate
- ■ Systems
- ☐ Trading
- ☐ Training
- ☐ Variable Contracts

Executive Summary

NASD Regulation, Inc. (NASD Regulation®) is announcing the replacement of the current PC FOCUS℠ application with a Web-based, Internet version. Web-based FOCUS will be available to members for the September 1999 FOCUS filing.

Please note that the PC FOCUS application, which operates through Sprint, will not be available for the September filing. In this regard, it is imperative that you immediately forward this *Notice* to the Financial & Operational Principal at your firm.

Questions concerning this *Notice* may be directed to Elizabeth Wollin, Member Regulation, NASD Regulation, at (301) 590-6743.

Preparing For Web-Based FOCUS

To prepare for filing monthly, quarterly, and annual FOCUS filing through Web-based FOCUS, members must complete the appropriate entitlement forms (*User Account Acknowledgment Form* and *Account Administrator Entitlement Form*—see below). The forms are being mailed to members. Members will not be able to access Web-based FOCUS until the entitlement forms are fully and accurately completed and submitted. Members must take the following steps:

- Read and execute the "User Account Acknowledgment Form (UAAF)." The original UAAF must be signed and returned to NASD Regulation *via* mail or courier. Faxed copies will not be accepted. Web-based FOCUS application utilizes the same entitlement functionality as the Web Central Registration Depository (CRD℠) system. The UAAF is a modified version of the form members completed to authorize Web CRD entitlement. Members may designate their Web CRD Account Administrator to also serve as their Web-based FOCUS Account Administrator.

- Complete and return the "Account Administrator Entitlement Form" so that specific privileges may be assigned to the Account Administrator.

Members must complete and submit these forms no later than **August 31, 1999**. If this deadline is missed, the setup of Web-based FOCUS accounts may be delayed. Once these forms are processed, a confirmation package will be sent to members' Account Administrators with user account and initial password information. For assistance in completing the entitlement forms, please call (800) 321-NASD.

System Highlights Of Web-Based FOCUS

- Create and submit FOCUS forms—Schedule I, Part II, and Part IIA.

- View a list of upcoming filing requirements.

- Print FOCUS filings from your printer.

- Upload a FOCUS filing from your computer.

- Access Web-based FOCUS from any workstation running either Microsoft's Internet Explorer 4.01 SP2 or Netscape's browser version 4.05 or higher. Members will not need to install any additional software on their workstation.

- Utilize the Secure Socket Layer (SSL) security built into your browser to protect your data.

- Access any historical FOCUS filings online.

- Download your filings in existing PC FOCUS format over the Internet to meet your company's record retention needs and submit the filings to other agencies.

- PIN numbers will no longer be required. However, users will have to be 'entitled' to access the application.

- Access is controlled using a user identification and password. Web-based FOCUS uses the same security mechanisms as Web CRD. A single individual may have his/her identification authorized to access both the CRD and FOCUS systems.

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NASD Notice to Members 99-71

Labor Day: Trade Date–Settlement Date Schedule

Labor Day: Trade Date-Settlement Date Schedule

The Nasdaq Stock Market® and the securities exchanges will be closed on Monday, September 6, 1999, in observance of Labor Day. "Regular way" transactions made on the business days noted below will be subject to the following schedule:

Trade Date	Settlement Date	Reg. T Date*
Aug. 31	Sept. 3	Sept. 8
Sept. 1	7	9
2	8	10
3	9	13
6	Markets Closed	—
7	10	14

*Pursuant to Sections 220.8(b)(1) and (4) of Regulation T of the Federal Reserve Board, a broker/dealer must promptly cancel or otherwise liquidate a customer purchase transaction in a cash account if full payment is not received within five business days of the date of purchase or, pursuant to Section 220.8(d)(1), make application to extend the time period specified. The date by which members must take such action is shown in the column titled "Reg. T Date."

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Suggested Routing

- ☐ Senior Management
- ☐ Advertising
- ☐ Continuing Education
- ☐ Corporate Finance
- ☐ Government Securities
- ☐ Institutional
- ☐ Insurance
- ■ Internal Audit
- ■ Legal & Compliance
- ■ Municipal
- ☐ Mutual Fund
- ■ Operations
- ☐ Options
- ☐ Registered Representatives
- ☐ Registration
- ☐ Research
- ■ Syndicate
- ■ Systems
- ■ Trading
- ☐ Training
- ☐ Variable Contracts

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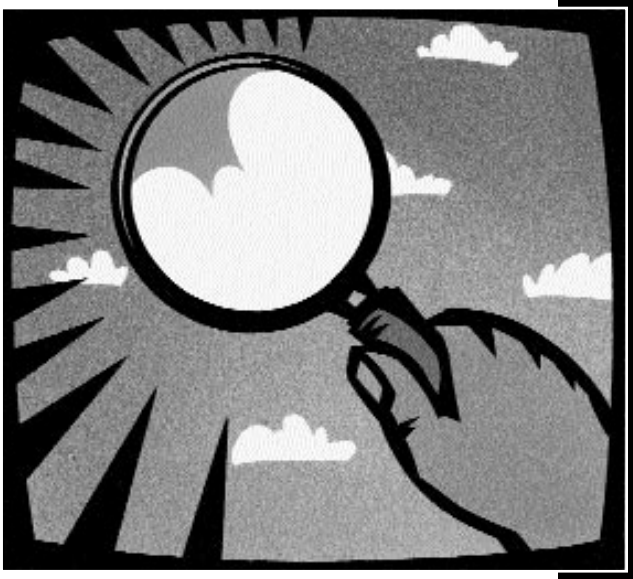

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- 33% of job applicants falsify their employment applications.
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- On average, employees embezzle more than $125,000.
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ADREM Profiles offers NASD members 60 research services at 30% off their standard prices.

For just $42* and within 1 to 4 days, you can verify:

- Previous Employment
- County Level Criminal (Felony and Misdemeanor)
- Pre-employment Credit
- Social Security Number

Drug tests are also available.

Visit ADREM's special NASD Web page at *www.adpro.com* and enter NASD as your ID and ADREM as your password. Or call 800-281-1250.

*Pricing for New York searches may be higher because of state court fees.

NASD Member Benefits

800-281-1250

To take advantage of these savings, be sure to mention your NASD membership.

NASD

Parent of The Nasdaq-Amex Market Group

NASD Notice to Members 99-72

Fixed Income Pricing System Additions, Changes, And Deletions As Of June 22, 1999

Suggested Routing

- ■ Senior Management
- □ Advertising
- □ Continuing Education
- ■ Corporate Finance
- □ Government Securities
- ■ Institutional
- □ Insurance
- □ Internal Audit
- ■ Legal & Compliance
- ■ Municipal
- □ Mutual Fund
- ■ Operations
- □ Options
- □ Registered Representatives
- □ Registration
- □ Research
- □ Syndicate
- ■ Systems
- ■ Trading
- □ Training
- □ Variable Contracts

As of June 22, 1999, the following bonds were added to the Fixed Income Pricing System℠ (FIPS®).

Symbol	Name	Coupon	Maturity
AWAS.GD	Allied Waste North American Inc.	7.625	01/01/06
BFIT.GB	Bally Total Fitness Holding Corp. Series D	9.875	10/15/07
CFTR.GA	Conseco Finl Trust III	8.796	04/01/27
CHCA.GF	Chancellor Media Corp.	8.000	11/01/08
CLSP.GA	Carrols Corp.	9.500	12/01/08
CMS.IH	CMS Energy Corp. Series B	6.750	01/15/04
COL.GI	Columbia/HCA Healthcare Corp.	6.410	06/15/00
COL.GJ	Columbia/HCA Healthcare Corp.	7.690	06/15/25
CQB.GI	Chiquita Brands Intl. Inc.	10.000	06/15/09
DAHX.GA	Decrane Aircraft Holdings Inc. Series B	12.000	09/30/08
DMNS.GA	Dominos Inc. Series B	10.375	01/15/09
DSYG.GA	Dobson/Sygnet Communications	12.250	12/15/08
FLO.GE	R&B Falcon Corp.	9.500	12/15/08
FLO.GF	R&B Falcon Series B	9.125	12/15/03
FPTU.GA	First America Cap Tr I	8.500	04/15/12
FTVC.GA	Frontiervision LP/Capital Series B	11.875	09/15/07
HPCA.GA	Hospital Corp. Amer	0.000	06/01/01
HPCA.GB	Hospital Corp. Amer	0.000	06/01/02
HSE.GC	H S Resources Inc.	9.250	11/15/06
ICIX.GG	Intermedia Communications Inc. Series B	12.250	03/01/09
ICIX.GH	Intermedia Communications Inc. Series B	9.500	03/01/09
INLP.GB	Insilco Holding Co. Series B	12.000	08/15/07
JIT.GA	Pentacon Inc. Series B	12.250	04/01/09
JORD.GG	Jordan Industries Inc. Series D	10.375	08/01/07
LVLT.GB	Level 3 Communications Inc.	10.500	12/01/08
MLWL.GB	Mail-Well I Corp. Series B	8.750	12/15/08
NTRP.GA	NTL Communications Corp. Series B	12.375	10/01/08
NTRP.GB	NTL Communications Corp. Series B	11.500	10/01/08
NXTL.GH	Nextel Communications Inc.	12.000	11/01/08
OGLE.GA	Oglebay Norton Co.	10.000	02/01/09
OXAU.GC	Oxford Automotive Inc. Series D	10.125	06/15/07
PAW.GA	Florida Panthers Holdings	9.875	04/15/09
PGHI.GA	Premier Graphics Inc.	11.500	12/01/05
PKS.GE	Premier Parks Inc.	9.750	06/15/07
PXCP.GA	Phoenix Color Corp.	10.375	02/01/09
TDGM.GA	Transdigm Inc.	10.375	12/01/08
THM.GA	Thermwood Corp.	12.000	04/27/14
UHSP.GB	Universal Hospital Svs Inc.	10.250	03/01/08
URI.GD	United Rentals Inc. Series B	9.250	01/15/09
VPI.GC	Vintage Petroleum Inc.	9.750	06/30/09
VRIO.GC	Verio Inc.	11.250	12/01/08
WRC.GA	World Color Press Inc.	7.750	02/15/09

As of June 22, 1999, the following bonds were deleted from FIPS.

Symbol	Name	Coupon	Maturity
AMMB.GD	Amresco Inc.	8.750	07/01/99
ANN.GC	Ann Taylor Inc.	8.750	06/15/00
CNLP.GB	Conn Light & Power Co.	7.250	07/01/99
CNLP.GC	Conn Light & Power Co.	7.375	12/01/25
CNLP.GD	Conn Light & Power Co.	5.750	07/01/00
CNLP.GG	Conn Light & Power Co.	6.125	02/01/04
CNLP.GJ	Conn Light & Power Co.	7.875	10/01/24
CNLP.GK	Conn Light & Power Co.	7.750	06/01/02
CPU.GA	CompUSA Inc.	9.500	06/15/00
GRYH.GA	Greystone Homes Inc.	10.750	03/01/04
GSNP.GA	Garden State Newspapers Inc.	12.000	07/01/04
LRGY.GA	LaSalle Energy Corp.	11.750	07/01/99
MCCC.GA	McCrory Corp.	7.770	07/15/94
MCCC.GD	McCrory Corp.	7.750	09/15/95
MGL.GA	Magellan Health Services Inc.	11.250	04/15/04
PAHD.GA	PA Holdings Corp.	13.750	07/15/99
PLTC.GB	Plastic Containers Inc.	10.000	12/15/06
RHR.GB	Rohr Industry Inc.	11.625	05/15/03
RYK.GA	Rykoff-Sexton Inc.	8.875	11/01/03
SHVC.GA	Shop Vac Corp.	10.625	09/01/03
TSXC.GA	Transco Energy Co.	11.250	07/01/99
USAR.OM	U.S. Air Inc. Series 88-B	10.180	06/27/99
USAR.ON	U.S. Air Inc. Series 88-C	10.180	06/27/99
USAR.OO	U.S. Air Inc. Series 88-A	10.180	06/27/99
USAR.OP	U.S. Air Inc. Series 88-D	10.180	06/27/99
WSIN.GA	Wesco International Inc. Series B	11.125	06/01/08

As of June 22, 1999, changes were made to the symbols of the following FIPS bonds:

New Symbol	Old Symbol	Name	Coupon	Maturity
BVC.GA	BVCC.GA	Bayview Capital Corp.	9.125	08/15/07

All bonds listed above are subject to trade-reporting requirements. Questions pertaining to FIPS trade-reporting rules should be directed to Stephen Simmes, Market Regulation, NASD Regulation®, at (301) 590-6451.

Any questions regarding the FIPS master file should be directed to Cheryl Glowacki, Nasdaq® Market Operations, at (203) 385-6310.

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NASD Notice to Members 99-73

NASD Requests Comment On Proposed Amendments To The Code Of Procedure And Other Provisions; Comment Period Expires **September 13, 1999**

Suggested Routing

- ■ Senior Management
- ☐ Advertising
- ☐ Continuing Education
- ☐ Corporate Finance
- ☐ Executive Representatives
- ☐ Government Securities
- ☐ Institutional
- ☐ Insurance
- ☐ Internal Audit
- ■ Legal & Compliance
- ☐ Municipal
- ☐ Mutual Fund
- ☐ Operations
- ☐ Options
- ☐ Registered Representatives
- ☐ Registration
- ☐ Research
- ☐ Syndicate
- ☐ Systems
- ☐ Trading
- ☐ Training
- ☐ Variable Contracts

Executive Summary

The National Association of Securities Dealers, Inc. (NASD® or Association) Code of Procedure (the Code) has been in place since August 7, 1997. In light of the Association's additional experience litigating matters under the Code, the Association is proposing a series of clarifying and substantive changes to the Code and other provisions as described more fully below. These changes include:

- setting forth more clearly the Department of Market Regulation's role in disciplinary proceedings;
- clarifying the authority of hearing officers and making some limited changes to that authority;
- clarifying the scope of the Association's document production requirements;
- providing for hearing panel review of staff determinations to impose limitations on member firms' business activities because of financial and/or operational difficulties;
- providing for changes to the process for appeals of disciplinary actions, statutory disqualification proceedings, and certain other accelerated proceedings;
- providing for a streamlined process to impose bars or expulsions for the failure to provide information to the Association; and
- providing for a process by which the Association can more expeditiously cancel memberships of firms that fail to meet the Association's eligibility and qualification standards.

Attachment A includes the text of the proposed changes.

Request For Comment

NASD Regulation encourages all interested parties to comment on the proposal. Comments must be received by **September 13, 1999**. Comments should be mailed to:

Joan Conley
Office of the Corporate Secretary
NASD Regulation, Inc.
1735 K Street, NW
Washington, DC 20006-1500

or e-mail to:
pubcom@nasd.com

Important Note: The only comments that will be considered are those submitted via e-mail or in writing.

Before becoming effective, any rule change developed as a result of comments received must be adopted by the NASD Regulation, Inc. (NASD Regulation®) Board of Directors, may be reviewed by the NASD Board of Governors, and must be approved by the Securities and Exchange Commission (SEC).

Questions/Further Information

As noted, written comments should be submitted to Joan Conley. Questions concerning this *Notice to Members—Request For Comment* may be directed to Eric Moss, Assistant General Counsel, NASD Regulation, at (202) 728-8982.

Discussion

The Code, implemented on August 7, 1997, provides detailed requirements governing NASD Regulation's process for:

(1) authorizing, litigating, and issuing disciplinary decisions;

(2) providing for appeals of those decisions;

(3) taking certain actions through categories of accelerated proceedings; and

(4) determining requests for relief from statutory disqualifications.

Since August 7, 1997, the Association staff has had significant experience under the Code and has noted certain areas that need to be clarified or changed.

Custodian Of The Record

Firms often list persons not associated with the firms as custodians of records on the SEC Form BDW, and then the Association has difficulty obtaining records when firms no longer conduct business. The Association is proposing to add a provision to its Conduct Rules that would require members to designate, as the custodians of the record on the Form BDW, persons who are associated with the firms at the time the Forms BDW are filed.

Eligibility Of Panel Members

In certain circumstances, the National Adjudicatory Council (NAC) or the Review Subcommittee of the NAC (Review Subcommittee) may appoint panels to conduct hearings. Under Rule 1015, only one panel member can be from the NAC, unless a panel member is also a former NASD Regulation Director or NASD Governor. The Association is proposing to eliminate this restriction.

Market Regulation's Role In Disciplinary Process

Both the Department of Market Regulation and the Department of Enforcement represent NASD Regulation in formal disciplinary matters under the Code. However, the disciplinary rules only refer to the Department of Enforcement as the representative of the Association in these matters. The Department of Market Regulation represents NASD Regulation under a delegation of authority from the Department of Enforcement. The Association is proposing amending the Code to clarify the Department of Market Regulation's role in the disciplinary process.

Investigations

The Rule 8220 Series permits the Department of Enforcement to initiate proceedings to suspend or cancel membership from the Association or suspend the association of a person with a member based upon the failure to provide information. These proceedings may be initiated for the failure to provide information pursuant to an Association request or the failure to make required filings with the Association, such as FOCUS reports, or to keep membership applications or supporting documents current. The Association is proposing to amend the Rule 8220 Series to:

(1) as discussed below (under the heading *Failure To Respond*), limit the use of Rule 8220 proceedings to address serious on-going violations concerning associated persons and members that fail to provide the Association with requested information; and

(2) limit the sanctions available under Rule 8220 proceedings to suspensions.

Finally, the Association is proposing to amend the service provision under the Rule 8220 Series to make it consistent with the service provision under the Rule 9530 Series, a similar rule series. The staff is proposing that both the Rule 8220 Series and the Rule 9530 Series service provisions permit personal service, service by facsimile, and service by overnight courier. The Association is further proposing to clarify that attempted delivery of a document by an overnight courier may count as service under these provisions.

Service Of Papers—Address Changes

Rule 9134(b)(1) states that service of papers on a natural person in a disciplinary hearing must be at the person's residential address as reflected in the Central Registration Depository (CRD℠). If the Association staff has actual knowledge that the person's CRD address is out of date, then in addition to serving at the residential address as reflected in the CRD, service should also be made at the person's last known residential address and the CRD address of the firm with which the person is associated or affiliated, if he/she is currently in the industry. The Association is proposing to modify the rule to permit adjudicators to waive the requirement of sending papers to CRD addresses when they are no longer valid, and there is a more current address available. This change would only relate to documents served on respondents after complaints have been served.

Further, the Association is proposing to amend Rule 9135(a) to clarify that complaints shall be deemed timely filed so long as they are either mailed or delivered to the Office of Hearing Officers within the two-year jurisdictional period, as outlined in the By-Laws.

Severance Of Cases

Rule 9214 authorizes the Chief Hearing Officer to order the consolidation of disciplinary hearings, but does not specifically refer to the authority of the Chief Hearing Officer to sever disciplinary proceedings. The Association is proposing to amend Rule 9214 to clarify that the Chief Hearing Officer has authority to sever disciplinary proceedings involving multiple respondents into one or more proceedings.

Producing Documents

The Association is proposing amendments to Rule 9253 to clarify the scope of the Association's document production requirements. Rule 9251(a) requires the Association staff to make available to respondents documents prepared or obtained by the staff in connection with the investigations that led to the institution of a disciplinary proceeding. Exceptions to the production requirements are listed in Rule 9251(b), and include examination and inspection reports and internal employee communications. Notwithstanding these exceptions, documents containing the staff's investigative techniques might become discoverable under Rule 9253 if staff members are called as witnesses during hearings. Rule 9253 requires Association staff to produce written statements made or adopted by staff members, if they relate to the subject matter of those persons' testimony. It also requires the staff to produce contemporaneously recorded recitals of oral statements made by witnesses, if those written statements are substantially verbatim.

The proposed modifications of Rule 9253 clarify that the only portions of routine examination or inspection reports, internal employee communications, and any other internal documents that are required to be produced, under this rule, are the portions outlining the substance of (and any conclusions regarding) oral statements made by persons who are not employees of the Association when evidence of those statements are offered by Association staff during disciplinary hearings.

Amending Complaints

The Association is proposing to modify its rules regarding amending complaints to more closely follow the Federal Rules of Civil Procedure (FRCP). The FRCP does not limit the types of amendments that may be made to complaints. NASD Rule 9212, however, only permits amendments to "new matters of fact or law." The Association is proposing to amend the rule to eliminate this restriction. Thus, for instance, under proposed rule change, the Association staff could amend complaints to include additional respondents. Further, the FRCP permits amendments to make complaints conform to the evidence presented. The Association is proposing to modify Rule 9212 to permit such amendments. Also, the FRCP states that amendments to complaints will be freely granted when justice so requires. The Association is proposing to amend Rule 9212 to state that amendments to complaints will be freely granted when justice so requires. Association staff will need to obtain hearing officer approval to amend complaints after answers have been filed.

Effective Dates Of Sanctions

CRD currently sets the time of the imposition of sanctions imposed under the Code by notifying respondents in writing when fines are due and of the effective date of suspensions. The Association is proposing to amend several provisions of the Code to clarify that the effective dates of sanctions are the dates set by the Association staff unless stated otherwise in orders, decisions, or settlement agreements.

Written Orders

Rule 9241(e) states that hearing officers shall enter written rulings or orders reciting any agreements reached and any procedural determinations made by hearing officers at pre-hearing conferences. The Association is proposing to modify this rule to clarify that, when court reporters are present and transcripts of pre-hearing conferences are prepared, hearing officers may deem such transcripts to be sufficient records of the orders in lieu of written orders.

Summary Dispositions

Rule 9264(a) authorizes either the Association or respondents to file motions to summarily dispose of "any or all the causes of action in the complaint." This rule, however, does not permit parties to move to eliminate issues that do not involve entire "causes of actions." The Association is proposing to modify Rule 9264(a) to track the language in the FRCP, which permits courts to dismiss factual issues.

Further, the Association is proposing to modify Rule 9264 to authorize hearing officers to deny, grant, or defer motions to dismiss without referring the matter to the full panel. The authority to grant such motions would be limited to jurisdictional issues, such as whether the complaint was filed within the two-year jurisdictional period.

Default Decisions

Rule 9269 provides that motions to set aside default decisions should be made to the Review Subcommittee or the NAC. The hearing officers who issue the default decisions, however, are particularly familiar with the issues presented. The staff is proposing to modify the rule to state that motions to set aside default decisions should be made to the hearing officers that originally decided the defaults. Appeals from such denials could be made to the NAC or the Review Subcommittee.

Remand Cases

Rule 9349 authorizes the NAC to remand disciplinary cases back to hearing panels. The Association is proposing to amend Rule 9344 and Rule 9349 to clarify that the Review Subcommittee may also remand disciplinary cases back to hearing panels.

Office Of General Counsel

Under Rule 9311 and Rule 9312, the General Counsel is required to obtain Review Subcommittee or NAC authorization to order parties to brief particular matters. The General Counsel rarely seeks additional briefing on particular points, but where the General Counsel believes that additional briefing is necessary, the Review Subcommittee or the NAC would most likely order it. Thus, requiring the General Counsel to seek authorization for additional briefing is an unnecessary use of resources. The Association is proposing that this provision be modified to eliminate this requirement. The Association proposes including in the rules a process by which parties may challenge, before the Review Subcommittee or the NAC, requests for additional briefing made by the General Counsel.

Briefing Schedules

Rule 9347(b) establishes briefing schedules for papers filed in NAC proceedings. The Association is proposing amending this rule to clarify that the time periods listed in the rule are only applicable to the principal briefing schedule and not applicable to the briefing of subsequent collateral issues.

Schedule For Board Submissions

The Association is proposing to amend Rule 9351 to eliminate the requirement that an NASD Governor needs to initiate the review of a disciplinary decision by the Board meeting that is at least 15 days after the date that the Board receives the proposed decision. The Association is proposing to amend the rule to state that if an NASD Governor decides to initiate a review of a disciplinary case, he/she should do so as soon as practicable, but no later than the second Board meeting following the transmission of material to the Board. Finally, the Association is proposing to amend the rule to state that the NASD Board should issue its decision as soon as practicable, but no later than the second Board meeting following the transmission of materials to the Board.

Procedures For Regulation Of Activities Of A Member Experiencing Financial Or Operational Difficulties

Under the Rule 9410 Series, the Department of Member Regulation issues notices and holds initial hearings to determine whether members must limit their business activities as a result of financial and/or operational difficulties. Members can appeal Member Regulation's decisions to the NAC, and the NAC or the Review Subcommittee will appoint a Subcommittee to participate in the review. The Association is proposing to amend the rule series to provide that firms may appeal limitations in notices issued by the Department of Member Regulation to hearing panels that will consist of a hearing officer and two other panelists. Under the proposal, the Department of Member Regulation would not hold hearings, and the NAC would not participate in matters handled under this rule series.

Currently, an NASD Governor may initiate the review of a decision issued by the NAC, under the Rule 9410 Series, not later than the next meeting of the NASD Board that is at least 15 days after the date on which the NASD Board receives the proposed written decision of the NAC. The Association is proposing to replace this procedure with a mechanism by which the Executive Committee of the NASD Board may initiate the review of the hearing panel decision for a period of 15 days. Currently, the Department of Member Regulation's decision is stayed unless otherwise ordered by the NAC decision. The Association is proposing to modify this provision to provide that the Department of Member Regulation's recommendation is stayed unless ordered otherwise by the Executive Committee.

Other Proceedings

Rule 9514(d)(2) states that proceedings involving the following need to be held within 21 days after respondents request hearings:

(i) the failure to pay an arbitration award or settlement agreement;

(ii) the denial of access to Association services; or

(iii) an advertising pre-use filing requirement.

Hearing panels may, during the initial 21-day period, extend the time an additional 21 days. The Association believes that these periods are too short, and is proposing to extend the initial period to 40 days, and the extension period to 30 days. Since suspensions are not in effect during the prehearing period, extending the period will not prejudice respondents.

Eligibility Proceedings

The Association is proposing several changes to the rules that govern the process by which

persons may become or remain associated with a member notwithstanding the existence of a statutory disqualification or for a current member or person associated with a member to obtain relief from the eligibility or qualification requirements. First, the eligibility rules do not state whether extensions of time or waivers of time limitations for filing of papers or holding of hearings may be granted. The Association is proposing to create a rule that permits such actions by consent of all the parties. Further, the eligibility rules do not state whether the disqualification hearing panel or the NAC may order that the record be supplemented. The Association is proposing to create such a rule.

The eligibility rules state that NASD Regulation's statutory disqualification recommendations become effective upon service on applicants. However, only the SEC can grant final approval of statutory disqualification applications. The Association is proposing to amend these rules to reflect this point.

If a member files an application for relief under the eligibility rules, the NAC or the Review Subcommittee appoints a hearing panel composed of two or more members who are current or former members of the NAC or former Directors or Governors. The Association is proposing that the rules be amended to state that members of the Statutory Disqualification Committee may also serve on hearing panels.

The eligibility rules state that if the Association staff initiated the proceedings, the Association will give to the applicant all documents that were relied on by the Association in issuing its notice. However, most applications are started by member firms, not the Association. The Association is proposing to amend the rules to reflect this fact.

The Association is also proposing to amend the rules to provide that once an application is filed, CRD will gather all of the information necessary to process the application, including:

(1) CRD records for the disqualified member, sponsoring member, and/or disqualified person, and the proposed supervisor; and

(2) all of the information submitted by the disqualified member or sponsoring member in support of the application.

The proposed rule would further provide that CRD will prepare an index of these documents, and simultaneously provide this index and copies of the documents to the disqualified member or sponsoring member, the Office of the General Counsel of NASD Regulation, and the Department of Member Regulation. The rule also would require the Department of Member Regulation to submit its recommendation and supporting documents to the hearing panel and the disqualified member or sponsoring member within 10 business days of the hearing, unless the parties otherwise agree. Similarly, the disqualified member or sponsoring member would be required to submit its documents to the hearing panel and the Department of Member Regulation within 10 business days of the hearing, unless otherwise agreed.

The amendments to the Rule 9520 Series concern the review procedures undertaken by Association staff in the case of certain disqualifying events. In particular, the Association is proposing to amend the rules to permit members to submit a written request for relief (rather than an MC-400 application) in cases where the disqualified member or person is subject to an injunction that was entered 10 or more years prior to the proposed admission or association. Under Exchange Act Rule 19h-1, the NASD is not required to provide any notice to the SEC of the proposed admission or association in these types of cases. The Association also proposes that members be able to file a written request for relief in cases where a member requests to change the supervisor of a disqualified person or where, for instance, the New York Stock Exchange (NYSE) has determined to approve the proposed association of a disqualified person and the NASD concurs with the determination. Member Regulation would also be granted discretion to approve the written request for relief in these cases, if it deemed such action to be consistent with the public interest and the protection of investors.

The Association also proposes to amend the Rule 9520 Series to permit Member Regulation to approve an MC-400 application for relief in those cases where the disqualifying event is excepted from the "full" notice requirements of Rule 19h-1, but where a "short form" notification to the SEC under Rule 19h-1 is still required. In these cases, the member would be required to file an MC-400, but Member Regulation would have the discretion to approve the application when consistent with the public interest and the protection of investors.

In addition, the Association is proposing new Rule 9523 to permit Member Regulation to recommend the membership or continued membership of a disqualified member or sponsoring member or the association or continuing association of a disqualified person pursuant to a supervisory plan. The procedures set forth in proposed Rule 9523 are modeled on current Rule 9216 concerning Acceptance, Waiver, and Consent procedures, and are intended to avoid the

requirement of a formal hearing and decision by the Statutory Disqualification Committee (and its hearing panels) in cases that generally involve only the issue of what type of supervisory plan is appropriate for the disqualified member or person. Under proposed Rule 9523, the member would be required to file an MC-400 application with the NASD. Member Regulation, however, would have the discretion to recommend the approval of the application in the event an appropriate supervisory plan is established. The member would be required to execute a letter consenting to the imposition of the supervisory plan. The letter and the supervisory plan would then be submitted to the Office of General Counsel and/or the Chairman of the Statutory Disqualification Committee for review and possible approval. While both the Office of General Counsel and the Committee Chairman would have authority to approve the application or refer it to the NAC, only the Committee Chairman would be permitted to reject the application.

Failure To Respond

As noted above (under the heading *Investigations*), proceedings initiated under the Rule 8220 Series are designed to address serious on-going violations concerning associated persons and members that are failing to provide the Association with information. For this reason, these proceedings are brought on an accelerated basis.

The Association is proposing to create a new rule series (Rule 9540 Series), which would be used against those who fail to provide the Association with information, required filings, or keep membership applications or supporting documents current. Under the proposed Rule 9540 Series, the Association would send notices informing respondents that failure to provide the Association with previously requested information or required filings or the failure to keep its membership application or supporting documents current will result in suspensions, unless the information is provided to the Association within 20 days. Respondents would have five days to request hearings to challenge proposed suspensions. These hearings would be conducted before three-member hearing panels, and the hearing panels would have the authority to order any fitting sanctions, including expulsions and bars. Respondents who fail to request hearings to challenge the suspension during the six-month period following the receipt of notices initiating proceedings under this rule series will be automatically barred or expelled.

Further, the Association is proposing to include in the Rule 9540 Series a process by which the Department of Member Regulation could quickly cancel the memberships of firms that fail to meet the Association's eligibility and qualification standards. Under the proposal, the Association would send letters to members informing them that their memberships will be canceled within 20 days of receipt of the letters, unless the firm becomes eligible for continuance in membership within this time period. The members will be provided opportunities to request hearings within five days of service of the notices to challenge the proposed cancellations. The hearings would be held before Hearing Officers.

ATTACHMENT A

Text Of Amendments

(Note: New text is underlined; deletions are bracketed.)

1000. MEMBERSHIP, REGISTRATION AND QUALIFICATION REQUIREMENTS

1010. Membership Proceedings

1015. Review by National Adjudicatory Council

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

(d) Appointment of Subcommittee

The National Adjudicatory Council or the Review Subcommittee defined in Rule 9120 shall appoint a Subcommittee to participate in the review. The Subcommittee shall be composed of [at least two members. One member shall be a current member of the National Adjudicatory Council. The remaining member or members shall be current or past Directors or past Governors.] two or more persons who shall be current or past members of the National Adjudicatory Council or former Directors or Governors.

3100. BOOKS AND RECORDS, AND FINANCIAL CONDITION

3121. Custodian of the Record

A member who files a Securities and Exchange Commission Form BDW shall designate on the Form BDW, as the custodian of the record, a person associated with the member at the time that the Form BDW is filed.

8000. INVESTIGATIONS AND SANCTIONS

8200. INVESTIGATIONS

8220. Suspension [or Cancellation] for Obstructing Investigations [Failure to Provide Requested Information]

8221. Notice

(a) Notice to Member

If a member fails to provide any information, report, material, data, or testimony requested pursuant to the NASD By-Laws or the Rules of the Association[, or fails to keep its membership application or supporting documents current], the Department of Enforcement or the Department of Market Regulation may provide written notice to such member specifying the nature of the failure and stating that the failure to take such action within 20 days after service of the notice constitutes grounds for suspension [or cancellation] of membership.

(b) Notice to Person Associated with Member

If a person associated with a member fails to provide any information, report, material, data, or testimony requested pursuant to the NASD By-Laws or the Rules of the Association, the Department of Enforcement or the Department of Market Regulation may provide written notice to such person specifying the nature of the failure and stating that the failure to take such action within 20 days after service of the notice constitutes grounds for suspending the association of the person with the member.

(c) Service of Notice

The Department of Enforcement or the Department of Market Regulation shall serve the member or person associated with a member with such notice via personal service or overnight [commercial] courier or by facsimile at location described in Rule 9134(b). Service by overnight courier shall be accomplished by sending the papers through an overnight courier service that generates a written confirmation of receipt or of attempts at delivery.

8222. Hearing

(a) Request for Hearing

Within five days after the date of service of a notice issued under Rule 8221, a member or person associated with a member served with a notice under Rule 8221(c) may file with the NASD Regulation Office of General Counsel a written request for an expedited hearing before a subcommittee of the National Adjudicatory Council. The request shall state with specificity why the member or associated person believes that there are insufficient grounds for suspension or [cancellation or] any other reason for setting aside the notice issued under Rule 8221.

(b) Hearing Procedures

(1) Appointment of Subcommittee

If a hearing is requested, the National Adjudicatory Council or the Review Subcommittee described in Rule 9120 shall appoint a subcommittee to conduct the hearing and decide whether the member or person associated with a member should be suspended [or canceled]. The subcommittee shall be composed of a current member of the National Adjudicatory Council and one or more current or former members of the National Adjudicatory Council[,] or former Governor or Director. [NASD Regulation Board, or NASD Board.]

(2) Time of Hearing

The hearing shall be held within

30 days after the date of service of the notice issued under Rule 8221. Not later than seven days before the hearing, the subcommittee shall serve the member or person associated with a member with written notice of the date and time of the hearing via overnight [commercial] courier or facsimile and notify the Department of Enforcement or the Department of Market Regulation of the date and time of the hearing.

(3) Transmission of Documents

Not later than seven days before the hearing, the Department of Enforcement or the Department of Market Regulation shall serve the member or person associated with a member via overnight [commercial] courier with all documents that were considered in connection with the decision to issue a notice under Rule 8221, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon the conclusion of any review by the Commission or the federal courts. The Department of Enforcement or the Department of Market Regulation shall provide a copy of the documents transmitted to the member or person associated with a member to the subcommittee.

(4) Counsel

The member or person associated with a member and the Department of Enforcement or the Department of Market Regulation may be represented by counsel at a hearing conducted under this Rule.

(5) Evidence

Formal rules of evidence shall not apply to a hearing under this Rule. Not later than four days before the hearing, the member or person associated with a member and the Department of Enforcement or the Department of Market Regulation shall exchange copies of proposed hearing exhibits and witness lists and provide copies of the same to the subcommittee.

(6) Witnesses No change.

(7) Additional Information

At any time during its consideration, the subcommittee may direct the member or person associated with a member or the Department of Enforcement or the Department of Market Regulation to submit additional information. Any additional information submitted shall be provided promptly to all parties at least one business day before the subcommittee renders its decision.

(8) through **(10)** No change.

8223. Decision

(a) Subcommittee

(1) Proposed Written Decision No change.

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

If no Governor calls the proceeding for review within the time prescribed in paragraph (b)(1), the subcommittee's proposed written decision shall become final, and the subcommittee shall serve the final written decision on the member or associated person via overnight [commercial] courier or facsimile.

(b) NASD Board of Governors

(1) Call For Review by Governor No change.

(2) Review and Decision

If a Governor calls the suspension or cancellation proceeding for review within the time prescribed in subparagraph (1), a review panel shall meet and conduct a review not later than 14 days after the call for review. The review panel shall be composed of the NASD Board Executive Committee, except that the Governor who calls the proceeding for review shall serve on the review panel in lieu of a member of the Executive Committee who has the same classification (Industry, Non-Industry, or Public) as such Governor. The review panel may affirm, modify, or reverse the decision of the subcommittee. Not later than seven days after the review panel meeting, the review panel shall serve a final written decision on the member or person associated with a member via overnight [commercial] courier or facsimile. The decision shall state the disposition of the suspension or cancellation proceeding, and if a suspension is imposed, state the grounds for the suspension and the conditions for terminating the suspension.

8225. Termination of Suspension

(a) Filing of Request

A suspended member or person associated with a member may file a written request for termination of the suspension on the ground of full compliance with the notice issued under Rule 8221 or, if applicable, the conditions of a decision under Rule 8223, with the head of the

department or office of the Association that filed the notices under Rule 8221 [Department of Enforcement].

(b) Response by Association Staff [Department of Enforcement]

The head of the department of the Association that filed the notice under Rule 8221 [Department of Enforcement] shall respond to the request in writing within five days after receipt of the request.

(1) Request Granted

If the head of the department or office [Department of Enforcement] grants the request, he or she shall serve the member or person associated with a member with written notice of the termination of the suspension via overnight [commercial] courier or facsimile.

(2) Request Denied

If the head of the department or office denies the request, the suspended member or person associated with a member may file a written request for relief with the NASD Regulation Office of General Counsel. If the member or person associated with a member files the written request for relief within 30 days after service of the decision under Rule 8223, the review panel constituted under Rule 8223 shall respond to the request for relief in writing within ten days after receipt of the request. If the member or person associated with a member files the written request for relief more than 30 days after service of the decision under Rule 8223, the National Adjudicatory Council shall respond to the request for relief in writing within ten days after receipt of the request. The review panel's or National Adjudicatory Council's response shall be served on the member or person associated with a member via overnight [commercial] courier or facsimile.

8300. SANCTIONS

8310. Sanctions for Violation of the Rules

IM-8310-2. Release of Disciplinary Information

(a) through (b) No Change.

(c) (1) The Association shall release to the public information with respect to any disciplinary complaint initiated by the Department of Enforcement or the Department of Market Regulation of NASD Regulation, Inc., the NASD Regulation, Inc. Board of Directors, or the NASD Board of Governors containing an allegation of a violation of a designated statute, rule or regulation of the Commission, NASD, or Municipal Securities Rulemaking Board, as determined by the NASD Regulation, Inc. Board of Directors (a "Designated Rule"); and may also release such information with respect to any disciplinary complaint or group of disciplinary complaints that involve a significant policy or enforcement determination where the release of information is deemed by the President of NASD Regulation, Inc. to be in the public interest.

(2) No change.

(d) through (g) No change.

[(h) If a final decision of the Association is not appealed to the Commission, the sanctions specified in the decision (other than bars and expulsions) shall become effective on a date established by the Association but not before the expiration of 30 days after the date of the decision. Bars and expulsions, however, shall become effective upon issuance of the decision, unless the decision specifies otherwise.]

(h)[(i)] If a decision of the Association imposing monetary sanctions of $10,000 or more or a penalty of expulsion, revocation, suspension and/or barring of a member from being associated with all members is appealed to the Commission, notice thereof shall be given to the membership and to the press as soon as possible after receipt by the Association of notice from the Commission of such appeal and the Association's notice shall state whether the effectiveness of the Board's decision has been stayed pending the outcome of proceedings before the Commission.

(i)[(j)] In the event an appeal to the courts is filed from a decision by the Commission in a case previously appealed to it from a decision of the Association, involving the imposition of monetary sanctions of $10,000 or more or a penalty of expulsion, revocation, suspension and/or barring of a member from being associated with all members, notice thereof shall be given to the membership as soon as possible after receipt by the Association of a formal notice of appeal. Such notice shall include a statement whether the order of the Commission has been stayed.

(j)[(k)] Any order issued by the Commission of revocation or suspension of a member's broker/dealer registration with the Commission; or the suspension or expulsion of a member from the Association; or the suspension or barring of a member or person associated with a member from association with all broker/dealers or membership; or the imposition of monetary sanctions of $10,000 or more shall be released to the public

through a notice containing the effective date thereof sent as soon as possible after receipt by the Association of the order of the Commission.

(k)[(l)] Cancellations of membership or registration pursuant to the Association's By-Laws, Rules and Interpretative Material shall be released to the public as soon after the effective date of the cancellation as possible.

(l)[(m)] Releases to the public referred to in paragraphs (c) and (d) above shall identify the Rules and By-Laws of the Association or the SEC Rules violated, and shall describe the conduct constituting such violation. Releases may also identify the member with which an individual was associated at the time the violations occurred if such identification is determined by the Association to be in the public interest.

9000. CODE OF PROCEDURE

9100. APPLICATION AND PURPOSE

9120. Definitions

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

(e) "Department of Enforcement"

The term "Department of Enforcement" means the Department of Enforcement of NASD Regulation [or its delegatee, the Department of Market Regulation].

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

(r) "Interested Association Staff"

The term "Interested Association Staff" means, in the context of:

(1) a disciplinary proceeding under the Rule 9200 Series and the Rule 9300 Series:

(A) the Head of Enforcement;

(B) an employee of the Department of Enforcement who reports, directly or indirectly, to the Head of Enforcement;

(C) an Association employee who directly participated in the authorization of the complaint; [or]

(D) an Association employee who directly participated in an examination, investigation, prosecution, or litigation related to a specific disciplinary proceeding, and a district director or department head to whom such employee reports;

(E) the Head of the Department of Market Regulation; or

(F) an employee of the Department of Market Regulation who reports, directly or indirectly, to the Head of the Department of Market Regulation;

(2) through (4) No change.

(s) through **(w)** No change.

(x) "Party"

With respect to a particular proceeding, the term "Party" means:

(1) in the Rule 9200 Series and the Rule 9300 Series, the Department of Enforcement or the Department of Market Regulation or a Respondent;

(2) through (4) No change.

(y) through **(bb)** No change.

9130. Service; Filing of Papers

9131. Service of Complaint and Document Initiating a Proceeding

(a) Service on Each Party

A complaint shall be served on each Party by the Department of Enforcement or the Department of Market Regulation. A document initiating a proceeding shall be served on each Party by the Party or person initiating such proceeding or his or her counsel or representative.

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

9134. Methods of, Procedures for Service

(a) Methods

(1) through (2) No change.

(3) Service by [Commercial] Courier

Service by [commercial] courier may be accomplished by sending the papers through an [commercial] courier service that generates a written confirmation of receipt or of attempts at delivery.

(b) Procedures

(1) Service on Natural Persons

Papers served on a natural person may be served at the natural person's residential address, as reflected in the Central Registration Depository, if applicable. When a Party or other person responsible for serving such person has actual knowledge that the natural person's Central Registration Depository address is out of date, duplicate copies shall be served on the natural person at the natural person's last known residential address and the

business address in the Central Registration Depository of the entity with which the natural person is employed or affiliated. Papers may also be served at the business address of the entity with which the natural person is employed or affiliated, as reflected in the Central Registration Depository, or at a business address, such as a branch office, at which the natural person is employed, or at which the natural person is physically present during a normal business day. The Hearing Officer may waive the requirement of serving documents (other than complaints) at the addresses listed in the Central Registration Depository if there is evidence that these addresses are no longer valid, and there is a more current address available. If a natural person is represented by counsel or a representative, papers served on the natural person, excluding a complaint or a document initiating a proceeding, shall be served on the counsel or representative.

(2) No change.

(3) When Service Is Complete

Personal service and service by [commercial] courier or express delivery are complete upon delivery. Service by mail is complete upon mailing.

9135. Filing of Papers with Adjudicator: Procedure

(a) When to File

Papers that are required to be filed with an Adjudicator within a time limit specified by the Adjudicator or within a time limit set forth in the Rules shall be deemed timely if received within the time limit, unless otherwise ordered by an Adjudicator, except complaints, which shall be deemed timely filed upon mailing or delivery to the Office of Hearing Officers. Other papers that are required to be filed shall be deemed timely if, on the same day such papers are served, they are also hand-delivered, mailed via U.S. Postal service first class mail, or sent by courier to the Association.

(b) Where to File

All papers required to be filed pursuant to the Rule 9200 Series and any notice of appeal or review required to be filed pursuant to the Rule 9300 Series shall be filed with the Office of Hearing Officers. All other papers required to be filed pursuant to the Rule 9000 Series shall be filed where specified in the Rule, or if not specified in the Rule, with the Adjudicator, unless the Adjudicator orders otherwise.

(c) Certificate of Service

Papers filed with an Adjudicator or the Office of Hearing Officers shall be accompanied by a certificate of service stating the name of the person or persons served, the date on which service is made, the method of service and, if service is not made in person, the address to which service is made. Such certificate shall be executed by the person who made the service. If the method of service on a Party is different from the method of service on any other Party, the certificate shall state why such different method was used.

9140. Proceedings

9146. Motions

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

(k) Motion For Protective Order

(1) A Party, a person who is the owner, subject, or creator of a Document subject to production under Rule 8210 or any other Rule which may be introduced as evidence in a disciplinary proceeding, or a witness who testifies at a hearing in a disciplinary proceeding may file a motion requesting a protective order to limit disclosure or prohibit from disclosure to other Parties, witnesses or other persons, except the Department of Enforcement and the Department of Market Regulation and other Association staff, Documents or testimony that contain confidential information. The motion shall include a general summary or extract of the Documents or testimony without revealing confidential details. If the movant seeks a protective order against disclosure to other Parties, copies of the Documents shall not be served on the other Parties. Unless the Documents are unavailable, the movant shall file for *in camera* inspection a sealed copy of the Documents for which the order is sought. If the movant is not a Party, the motion shall be served on each Party by the movant using a method in Rule 9134(a) and filed with the Adjudicator. A motion for a protective order shall be granted only upon a finding that disclosure of the Document or testimony would have a demonstrated adverse business effect on the movant or would involve an unreasonable breach of the movant's personal privacy.

(2) No change.

(l) General No change.

9200. DISCIPLINARY PROCEEDINGS

9210. Complaint and Answer

9211. Authorization of Complaint

(a) Complaint

(1) If the Department of Enforcement or the Department of Market Regulation believes that any NASD member or associated person is violating or has violated any rule, regulation, or statutory provision, including the federal securities laws and the regulations thereunder, which the Association has jurisdiction to enforce, the Department of Enforcement or the Department of Market Regulation may request authorization from the Office of Disciplinary Affairs to issue a complaint.

(2) The NASD Regulation Board and the NASD Board each shall have the authority to direct the Office of Disciplinary Affairs to authorize and the Department of Enforcement or the Department of Market Regulation to issue a complaint when, on the basis of information and belief, either of such boards is of the opinion that any NASD member or associated person is violating or has violated any rule, regulation, or statutory provision, including the federal securities laws and the regulations thereunder, which the Association has jurisdiction to enforce.

(b) Commencement of Disciplinary Proceeding No change.

9212. Complaint Issuance — Requirements, Service, Amendment, Withdrawal, and Docketing

(a) Form, Content, Notice, Docketing, and Service

(1) If a complaint is authorized, the Department of Enforcement or the Department of Market Regulation shall issue the complaint. Each complaint shall be in writing and signed by the Department of Enforcement or the Department of Market Regulation. The complaint shall specify in reasonable detail the conduct alleged to constitute the violative activity and the rule, regulation, or statutory provision the Respondent is alleged to be violating or to have violated. If the complaint consists of several causes of action, each cause shall be stated separately. Complaints shall be served by the Department of Enforcement or the Department of Market Regulation on each Party pursuant to Rules 9131 and 9134, and filed at the time of service with the Office of Hearing Officers pursuant to Rules 9135, 9136, and 9137.

(2) At the time of issuance of a complaint, the Department of Enforcement or the Department of Market Regulation may propose:

(A) an appropriate location for the hearing; and

(B) if the complaint alleges at least one cause of action involving a violation of a statute or a rule described in Rule 9120(s), that the Chief Hearing Officer select a Market Regulation Committee Panelist for the Hearing Panel, or, if applicable, the Extended Hearing Panel as described in Rule 9231.

(b) Amendments to Complaint

The Department of Enforcement or the Department of Market Regulation may file and serve an amended complaint [that includes new matters of fact or law] once as a matter of course at any time before the Respondent answers the complaint. Otherwise, upon motion by the Department of Enforcement or the Department of Market Regulation, the Hearing Officer may permit the Department of Enforcement or the Department of Market Regulation to amend the complaint, including amendments so as to make the complaint conform to the evidence presented [to include new matters of fact or law], after considering whether the Department of Enforcement or the Department of Market Regulation has shown good cause for the amendment and whether any Respondent will suffer any unfair prejudice if the amendment is allowed. Amendments to complaints will be freely granted when justice so requires.

(c) Withdrawal of Complaint

With prior leave of the Hearing Officer, the Department of Enforcement or the Department of Market Regulation may withdraw a complaint. If the Department of Enforcement or the Department of Market Regulation withdraws the complaint before the earlier of (1) the Hearing Panel's or, if applicable, the Extended Hearing Panel's, issuance of a ruling on a motion for summary disposition, or (2) the start of the hearing on the merits, the withdrawal of the complaint by the Department of Enforcement or the Department of Market Regulation shall be without prejudice and the Department of Enforcement or the Department of Market Regulation shall be permitted to refile a case based on allegations concerning the same facts and circumstances that are set forth in the withdrawn complaint. If the Department of Enforcement or the Department of Market Regulation requests to withdraw such complaint after the occurrence of either of the two events set forth in (1) and (2) in this paragraph, the Hearing Panel or, if applicable, the Extended Hearing Panel, after considering the facts and circumstances of the request, shall determine whether the withdrawal shall be granted with prejudice.

(d) Disciplinary Proceeding Docket No change.

9213. Assignment of Hearing Officer and Appointment of Panelists to Hearing Panel or Extended Hearing Panel

(a) Assignment of Hearing Officer

As soon as practicable after the Department of Enforcement or the Department of Market Regulation has filed a complaint with the Office of Hearing Officers, the Chief Hearing Officer shall assign a Hearing Officer to preside over the disciplinary proceeding and shall serve the Parties with notice of the Hearing Officer's assignment pursuant to Rule 9132.

(b) Appointment of Panelists No change.

9214. Consolidation or Severance of Disciplinary Proceedings

(a) Consolidation Initiated by Chief Hearing Officer

No change.

(b) Consolidation Initiated by a Party

No change.

(c) Impact on Hearing Panel or Extended Hearing Panel of Consolidation

No change.

(d) Severance Initiated by Chief Hearing Officer

The Chief Hearing Officer may order the severance of a disciplinary proceeding into two or more disciplinary proceedings, upon his or her own motion. In determining whether to order the severance of such disciplinary proceedings, the Chief Hearing Officer shall consider:

(1) whether the same or similar evidence reasonably would be expected to be offered at each of the possible hearings;

(2) whether the severance would conserve the time and resources of the Parties; and

(3) whether any unfair prejudice would be suffered by one or more Parties if the severance is (not) ordered.

If the Chief Hearing Officer proposes to sever a disciplinary proceeding, the Chief Hearing Officer shall serve upon the Parties notice of the proposed severance of disciplinary proceedings pursuant to Rule 9132. The Parties shall have 14 days after service to file a response, stating any arguments in favor of or opposition to severance.

(e) Severance Initiated by a Party

A Party may file a motion to sever a disciplinary proceeding if one or more of the factors favoring severance set forth in paragraph (d) appear to be present. If a Party moves to sever a disciplinary proceeding, the Party shall file such motion with the Office of Hearing Officers, and, pursuant to Rule 9133, shall serve the same upon each of the parties to the action proposed to be severed. The Parties shall have 14 days after service to file a response, stating any arguments in favor of or opposition to severance, and shall serve the response upon the Parties in the case proposed to be severed. The Chief Hearing Officer shall issue an order approving or denying the request for severance.

(f) Impact on Hearing Panel or Extended Hearing Panel of Severance

If the Chief Hearing Officer issues an order to sever a disciplinary proceeding for which a Hearing Panel or, if applicable, Extended Hearing Panel, has been appointed, the Chief Hearing Officer's order shall specify whether the same Hearing Panel or, if applicable, Extended Hearing Panel, shall preside over the severed disciplinary proceedings, or shall appoint a new Hearing Panel(s) or, if applicable, Extended Hearing Panel(s), to preside over any or all of the severed proceedings, based on the criteria set forth in Rules 9231 and 9232.

9215. Answer to Complaint

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

(f) Failure to Answer, Default

If a Respondent does not file an answer or make any other filing or request related to the complaint with the Office of Hearing Officers within the time required, the Department of Enforcement or the Department of Market Regulation shall send a second notice to such Respondent requiring an answer within 14 days after service of the second notice. The second notice shall state that failure of the Respondent to reply within the period specified shall allow the Hearing Officer, in the exercise of his or her discretion, pursuant to Rule 9269 to: (1) treat as admitted by the Respondent the allegations in the complaint; and (2) issue a default decision against the Respondent. If the Respondent fails to file an answer with the Office of Hearing Officers within the time required, the Hearing Officer may issue a default decision against the Respondent pursuant to Rule 9269.

9216. Acceptance, Waiver, and Consent; Plan Pursuant to SEC Rule 19d-1(c)(2)

(a) Acceptance, Waiver, and Consent Procedures

(1) Notwithstanding Rule 9211, if the Department of Enforcement or the Department of Market Regulation has reason to believe a violation has occurred and the member or associated person does not dispute the violation, the Department of Enforcement or the Department of Market Regulation may prepare and request that the member or associated person execute a letter accepting a finding of violation, consenting to the imposition of sanctions, and agreeing to waive such member's or associated person's right to a hearing before a Hearing Panel or, if applicable, an Extended Hearing Panel, and any right of appeal to the National Adjudicatory Council, the Commission, and the courts, or to otherwise challenge the validity of the letter, if the letter is accepted. The letter shall describe the act or practice engaged in or omitted, the rule, regulation, or statutory provision violated, and the sanction or sanctions to be imposed. Unless the letter states otherwise, the effective date of any sanction(s) imposed will be a date to be determined by the Association staff.

(2) through (4) No change.

(b) Procedure for Violation Under Plan Pursuant to SEC Rule 19d-1(c)(2)

(1) Notwithstanding Rule 9211, NASD Regulation or the National Adjudicatory Council may, subject to the requirements set forth in subparagraphs (b)(2) through (b)(4) and in SEC Rule 19d-1(c)(2), impose a fine (not to exceed $2,500) and/or a censure on any member or associated person with respect to any rule listed in IM-9216. If the Department of Enforcement or the Department of Market Regulation has reason to believe a violation has occurred and if the member or associated person does not dispute the violation, the Department of Enforcement or the Department of Market Regulation may prepare and request that the member or associated person execute a minor rule violation plan letter accepting a finding of violation, consenting to the imposition of sanctions, and agreeing to waive such member's or associated person's right to a hearing before a Hearing Panel or, if applicable, an Extended Hearing Panel, and any right of appeal to the National Adjudicatory Council, the Commission, and the courts, or to otherwise challenge the validity of the letter, if the letter is accepted. The letter shall describe the act or practice engaged in or omitted, the rule, regulation, or statutory provision violated, and the sanction or sanctions to be imposed. Unless the letter states otherwise, the effective date of any sanction(s) imposed will be a date to be determined by the Association staff.

(2) through (4) No change.

9240. Pre-hearing Conference and Submission

9241. Pre-hearing Conference

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

(e) Pre-hearing Order

At or following the conclusion of any conference held pursuant to this Rule, the Hearing Officer shall enter a written ruling or order that recites any agreements reached and any procedural determinations made by the Hearing Officer. However, if a court reporter prepares a transcript of the conference, the Hearing Officer may determine that it is unnecessary to issue a written ruling or order.

(f) Failure to Appear: Default No change.

9250. Discovery

9251. Inspection and Copying of Documents in Possession of Staff

(a) Documents to be Available for Inspection and Copying

(1) Unless otherwise provided by this Rule, or by order of the Hearing Officer, the Department of Enforcement or the Department of Market Regulation shall make available for inspection and copying by any Respondent, Documents prepared or obtained by Interested Association Staff in connection with the investigation that led to the institution of proceedings. Such Documents include but are not limited to:

(A) through (E) No change.

(2) The Department of Enforcement or the Department of Market Regulation shall promptly inform the Hearing Officer and each other Party if, after the issuance of a complaint, requests for information under Rule 8210 are issued under the same investigative file number under which the investigation leading to the institution of disciplinary proceedings was conducted. If Interested Association Staff receives Documents pursuant to a request for information under Rule 8210 after Documents have been made available to a Respondent for inspection and copying as set forth in paragraph (a), and if such Documents are material and relevant to the disciplinary proceeding in which such

Respondent is a Party, the additional Documents shall be made available to the Respondent not later than 14 days after the Interested Association Staff receives such Documents. If a hearing on the merits is scheduled to begin, Interested Association Staff shall make the additional Documents available to the Respondent not less than ten days before the hearing. If Interested Association Staff receives such Documents ten or fewer days before a hearing on the merits is scheduled to begin or after such hearing begins, Interested Association Staff shall make the additional Documents available immediately to the Respondent.

(3) Nothing in subparagraph (a)(1) shall limit the discretion of the Department of Enforcement or the Department of Market Regulation to make available any other Document or the authority of the Hearing Officer to order the production of any other Document.

(b) Documents That May Be Withheld

(1) The Department of Enforcement or the Department of Market Regulation may withhold a Document if:

(A) through (D) No change.

(2) Nothing in subparagraph (b)(1) authorizes the Department of Enforcement or the Department of Market Regulation to withhold a Document, or a part thereof, that contains material exculpatory evidence.

(c) Withheld Document List

The Hearing Officer may require the Department of Enforcement or the Department of Market Regulation to submit to the Hearing Officer a list of Documents withheld pursuant to subparagraphs (b)(1)(A) through (D) or to submit to the Hearing Officer any Document withheld. Upon review, the Hearing Officer may order the Department of Enforcement or the Department of Market Regulation to make the list or any Document withheld available to the other Parties for inspection and copying. A motion to require the Department of Enforcement or the Department of Market Regulation to produce a list of Documents withheld pursuant to paragraph (b) shall be based upon some reason to believe that a Document is being withheld in violation of the Code.

(d) Timing of Inspection and Copying

The Hearing Officer shall determine the schedule of production of documents pursuant to this Rule. Unless otherwise ordered by the Hearing Officer, the Department of Enforcement or the Department of Market Regulation shall commence making Documents available to a Respondent for inspection and copying pursuant to this Rule not later than 21 days after service of the Respondent's answer or, if there are multiple Respondents, not later than 21 days after the last timely answer is filed. If a Respondent in a multi-Respondent case fails to answer, the Department of Enforcement or the Department of Market Regulation shall make Documents available to all other Respondents not later than the later of:

(1) 21 days after the filing date of the last timely answer, or

(2) the expiration of the second period provided for filing an answer as set forth in Rule 9215(f).

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

(g) Failure to Make Documents Available — Harmless Error

In the event that a Document required to be made available to a Respondent pursuant to this Rule is not made available by the Department of Enforcement or the Department of Market Regulation, no rehearing or amended decision of a proceeding already heard or decided shall be required unless the Respondent establishes that the failure to make the Document available was not harmless error. The Hearing Officer, or, upon appeal or review, a Subcommittee, an Extended Proceeding Committee, or the National Adjudicatory Council, shall determine whether the failure to make the document available was not harmless error, applying applicable Association, Commission, and federal judicial precedent.

9253. Production of Witness Statements

(a) Availability

Notwithstanding the provisions of Rule 9251(b),

(1) A Respondent in a disciplinary proceeding may file a motion requesting that the Department of Enforcement or the Department of Market Regulation produce for inspection and copying any statement of any person called or to be called as a witness by the Department of Enforcement or the Department of Market Regulation that pertains, or is expected to pertain, to his or her direct testimony and which is "a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement made by

said witness and recorded contemporaneously with the making of such oral statement," as that phrase is used in 18 U.S.C. § 3500(e)(2).

(2) A Respondent in a disciplinary proceeding may also file a motion requesting that the Department of Enforcement or the Department of Market Regulation produce for inspection and copying any contemporaneously written statement made by an Interested Association Staff member during a routine examination or inspection about the substance of oral statements made by a non-Association person when (a) either the Interested Association Staff member or non-Association person is called as a witness by the Department of Enforcement or the Department of Market Regulation, and (b) that portion of the statement for which production is sought directly relates to the Interested Association Staff member's testimony or the testimony of the non-Association witness.

[A Respondent in a disciplinary proceeding may file a motion requesting that the Department of Enforcement produce for inspection and copying any statement of any person called or to be called as a witness by the Department of Enforcement that pertains, or is expected to pertain, to his or her direct testimony and that would be required to be produced pursuant to the Jencks Act, 18 U.S.C. § 3500. The production shall be made at a time and place fixed by the Hearing Officer and shall be made available to all Parties. Such production shall be made under conditions intended to preserve the items to be inspected or copied.]

(b) Failure to Produce — Harmless Error

In the event that a statement required to be made available for inspection and copying by a Respondent is not provided by the Department of Enforcement or the Department of Market Regulation, there shall be no rehearing of a proceeding already heard, or issuance of an amended decision in a proceeding already decided, unless the Respondent establishes that the failure to provide the statement was not harmless error. The Hearing Officer, or upon appeal or review, a Subcommittee, an Extended Proceeding Committee, or the National Adjudicatory Council, shall determine whether the failure to provide any statement was not harmless error, applying applicable Association, Commission, and federal judicial precedent.

9260. Hearing and Decision

9264. Motion for Summary Disposition

(a) Pre-hearing

After a Respondent's answer has been filed and Documents have been made available to that Respondent for inspection and copying pursuant to Rule 9251, the Respondent or the Department of Enforcement or the Department of Market Regulation, without leave of the Hearing Officer, may make a motion for summary disposition of any or all the causes of action in the complaint with respect to that Respondent, as well as any defense raised in a Respondent's answer. All pre-hearing motions for summary disposition and supporting papers shall be filed at least 21 days before the time set for the hearing, or at such earlier time as ordered by the Hearing Officer. Notwithstanding the provisions of Rule 9146(d), any opposition or response to a pre-hearing motion for summary disposition shall be filed at least seven days before the time set for the hearing.

(b) After Commencement of Hearing on Merits

After a hearing on the merits has commenced, a Respondent or the Department of Enforcement or the Department of Market Regulation may make a motion for summary disposition of any or all of the causes of action in the complaint with respect to that Respondent or defenses raised in that Respondent's answer only with leave of the Hearing Officer.

(c) Case Not Fully Adjudicated on Motion

If on motion under this rule a decision is not rendered upon the whole case or for all the relief asked and a hearing is necessary, the Hearing Panel or, if applicable, the Extended Hearing Panel, at the hearing of the motion, by examining the pleadings and the evidence before it and by questioning counsel, shall, if practicable ascertain what material facts exist without substantial controversy and what material facts are actually and in good faith controverted. It shall thereupon make an order specifying the facts that appear without substantial controversy, and directing such further proceedings in the action as are just. Upon the hearing of the action the facts so specified shall be deemed established, and the hearing shall be conducted accordingly.

(d) Form of Papers

A motion for summary disposition pursuant to paragraph (a) shall be accompanied by the following: a statement of undisputed facts; a supporting memorandum of points and authorities; and affidavits or declarations that set forth such facts as would be admissible at the hearing and show affirmatively that the affiant is competent to testify to the matters stated therein. A memorandum of points and

authorities in support or opposition shall not exceed 35 pages.

(e) [(d)] Rulings on Motion

The Hearing Officer may promptly deny or defer decisions on any motion for summary disposition, however, only the Hearing Panel or, if applicable, the Extended Hearing Panel, may grant a motion for summary disposition, except the Hearing Officer may grant motions for summary disposition with respect to questions of jurisdiction. [The Hearing Panel or, if applicable, the Extended Hearing Panel, shall promptly grant or deny the motion for summary disposition or shall defer decision on the motion.] The Hearing Panel or, if applicable, the Extended Hearing Panel, may grant the motion for summary disposition if there is no genuine issue with regard to any material fact and the Party that files the motion is entitled to summary disposition as a matter of law. If a Party files a motion under paragraph (a), the facts alleged in the pleadings of the Party against whom the motion is made shall be taken as true, except as modified by stipulations or admissions made by the non-moving Party, by uncontested affidavits or declarations, or by facts officially noticed pursuant to Rule 9145. If a Party opposing a motion for summary disposition made under paragraph (a) cannot present, by affidavit prior to the hearing, facts essential to justify the Party's opposition to the motion, the Hearing Panel or, if applicable, the Extended Hearing Panel, may deny the motion for summary disposition or defer the decision on the motion.

9268. Decision of Hearing Panel or Extended Hearing Panel

(a) Majority Decision No change.

(b) Contents of Decision

The decision shall include:

(1) through (5) No change.

(6) a statement describing any sanction imposed, the reasons therefor, and the date upon which such sanction shall become effective. Unless otherwise provided in the decision, the sanction(s) shall become effective on a date to be determined by Association staff.

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

9269. Default Decisions

(a) Issuance of Default Decisions

(1) No change.

(2) If the defaulting Party is the Respondent, the Hearing Officer may deem the allegations against that Respondent admitted. If the defaulting Party is the Department of Enforcement or the Department of Market Regulation, the Hearing Officer may issue a default decision ordering that the complaint be dismissed with prejudice.

(3) No change.

(b) Contents of Decision No change.

(c) Review of Default Decision

Party may, for good cause shown, file a motion to set aside a default, dismissal, and the imposition of costs. Upon a showing of good cause, the Hearing Officer that entered the original order shall decide the motion. [either the Review Subcommittee or the National Adjudicatory Council may enter such an order.] If the Hearing Officer that issued the original order is not available, the Chief Hearing Officer shall appoint another Hearing Officer to decide the motion.

(d) Final Disciplinary Action of the Association; Effectiveness of Sanctions

If a default decision is not appealed pursuant to Rule 9311 or called for review pursuant to Rule 9312 within 25 days after the date the Office of Hearing Officers serves it on the Parties, the default decision shall become the final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1). Unless otherwise provided in the default decision, the sanction(s) shall become effective on a date to be determined by the Association staff [30 days after the default decision becomes the final disciplinary action of the Association], except that a bar or expulsion shall become effective immediately upon the default decision becoming the final disciplinary action of the Association. The Association shall serve the decision on a Respondent by [overnight] courier, facsimile or other means reasonably likely to obtain prompt service when the sanction is a bar or an expulsion.

9270. Settlement Procedure

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

(c) Content and Signature Requirements

An offer of settlement shall be in writing and signed by the person making the offer, and, if the person is represented by counsel or a representative, signed also by the counsel or representative. The offer of settlement shall contain in reasonable detail:

(1) through (3) No change.

(4) a statement consenting to findings of fact and violations consistent with the statements contained in the offer of settlement required by subparagraphs (c)(2) and (c)(3); [and,]

(5) a proposed sanction to be imposed that is consistent with the Association's then current sanction guidelines or, if inconsistent with the sanction guidelines, a detailed statement supporting the proposed sanction; and,[.]

(6) the effective date of any sanction(s) imposed, or a statement that the effective date of the sanction(s) will be a date to be determined by the Association staff.

(d) Waiver No change.

(e) Uncontested Offers of Settlement

If a Respondent makes an offer of settlement and the Department of Enforcement or the Department of Market Regulation does not oppose it, the offer of settlement is uncontested. If an offer of settlement is determined to be uncontested by the Department of Enforcement or the Department of Market Regulation before a hearing on the merits has begun, the Department of Enforcement or the Department of Market Regulation shall transmit the uncontested offer of settlement and a proposed order of acceptance to the National Adjudicatory Council with its recommendation. If an offer of settlement is determined to be uncontested by the Department of Enforcement or the Department of Market Regulation after a hearing on the merits has begun, the Department of Enforcement or the Department of Market Regulation shall transmit the offer of settlement and a proposed order of acceptance to the Hearing Panel or, if applicable, the Extended Hearing Panel for acceptance or rejection. If accepted by the Hearing Panel or, if applicable, Extended Hearing Panel, the offer of settlement and the order of acceptance shall be forwarded to the National Adjudicatory Council to accept or reject.

(1) through (3) No change.

(f) Contested Offers of Settlement

If a Respondent makes an offer of settlement and the Department of Enforcement or the Department of Market Regulation opposes it, the offer of settlement is contested. When the Department of Enforcement or the Department of Market Regulation opposes an offer of settlement, the Respondent's written offer and the Department of Enforcement's or the Department of Market Regulation's written opposition shall be submitted to a Hearing Panel or, if applicable, an Extended Hearing Panel. The Hearing Panel or, if applicable, the Extended Hearing Panel, may order the Department of Enforcement or the Department of Market Regulation and the Respondent to attend a settlement conference.

(1) through (3) No change.

(g) through **(j)** No change.

9300. REVIEW OF DISCIPLINARY PROCEEDING BY NATIONAL ADJUDICATORY COUNCIL AND NASD BOARD; APPLICATION FOR COMMISSION REVIEW

9310. Appeal to or Review by National Adjudicatory Council

9311. Appeal by Any Party; Cross-Appeal

(a) Time to File Notice of Appeal

A Respondent or the Department of Enforcement or the Department of Market Regulation may file a written notice of appeal within 25 days after service of a decision issued pursuant to Rule 9268 or Rule 9269.

(b) through **(d)** No change.

(e) Waiver of Issues Not Raised

The National Adjudicatory Council may, in its discretion, deem waived any issue not raised in the notice of appeal or cross-appeal. The National Adjudicatory Council, the Review Subcommittee, a Subcommittee, the General Counsel or, if applicable, an Extended Proceeding Committee, [or, for a disciplinary proceeding decided under Rule 9269, the General Counsel,] shall provide the Parties with notice of, and an opportunity to submit briefs on, any issue that shall be considered by the National Adjudicatory Council if such issue was not previously set forth in the notice of appeal. Parties may submit motions to either the Review Subcommittee or the National Adjudicatory Council challenging requests for briefing made by the General Counsel under this Rule of issues that were not previously set forth in the notice of appeal.

(f) Withdrawal of Notice of Appeal or Cross-Appeal No change.

9312. Review Proceeding Initiated By National Adjudicatory Council

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

(c) Requirements

(1) No change.

(2) The statement contained in the notice of review shall not limit the scope of the National Adjudicatory Council's authority under Rule 9346 to review any issues raised in the record. The National Adjudicatory Council, the Review Subcommittee, a Subcommittee, the General Counsel or, if applicable, an Extended Proceeding

Committee, [or, for a disciplinary proceeding decided under Rule 9269, the General Counsel] shall provide the Parties with notice of, and an opportunity to submit briefs on, any issue that shall be considered by the National Adjudicatory Council if such issue was not previously set forth in the notice of review. Parties may submit motions to either the Review Subcommittee or the National Adjudicatory Council challenging requests for briefing made by the General Counsel under this Rule of issues that were not previously set forth in the notice of appeal.

(d) Effect of Withdrawal of Notice of Appeal, Cross-Appeal

If the review of a disciplinary proceeding by the National Adjudicatory Council is terminated before the National Adjudicatory Council issues a decision on the merits because all appealing Parties file a notice of withdrawal of appeal and no Party previously filed a notice of cross-appeal, or all Parties who previously filed a notice of cross-appeal file a notice of withdrawal of cross-appeal:

(1) No change.

(2) the General Counsel shall have the right to call for review a decision issued pursuant to Rule 9269 in accordance with Rule 9312(a)(2), except that the 25 [45] day period during which a call for review may be made shall begin on the day the Association receives the last filed notice of withdrawal of appeal or, if applicable, the last filed notice of withdrawal of cross-appeal.

9313. Counsel to National Adjudicatory Council

(a) Authority

[A Counsel to the National Adjudicatory Council shall be appointed by the General Counsel for each disciplinary case on appeal or review.] A Counsel to the National Adjudicatory Council shall have authority to take ministerial and administrative actions to further the efficient administration of a proceeding, including the authority to:

(1) through (7) No change.

(b) Review No change.

9340. Proceedings

9344. Failure to Participate Below; Abandonment of Appeal

(a) Failure to Participate Below

When an appealing Party did not participate in the disciplinary proceeding before a Hearing Officer, a Hearing Panel or, if applicable, an Extended Hearing Panel, but shows good cause for the failure to participate, the National Adjudicatory Council or the Review Subcommittee may dismiss the appeal and remand the matter for further proceedings, or may order that the appeal proceed. If the appealing Party did not participate in the disciplinary proceeding before a Hearing Officer, a Hearing Panel or, if applicable, an Extended Hearing Panel, and fails to show good cause for the failure to participate, the matter shall be considered by the Subcommittee or, if applicable, the Extended Proceeding Committee, and the National Adjudicatory Council on the basis of the record and other documents, as provided in Rules 9346 and 9347. Alternatively, the National Adjudicatory Council or Review Subcommittee may remand the disciplinary proceeding with instructions. For purposes of this paragraph, failure to participate shall include failure to file an answer or otherwise respond to a complaint, or failure to appear at a scheduled hearing, but shall not include failure to request a hearing pursuant to Rule 9221.

(b) Abandonment of Appeal No change.

9347. Filing of Papers in National Adjudicatory Council Proceedings

(a) Briefs; Reply Briefs; Requirements No change.

(b) Timely Filing of Briefs

Briefs shall be due upon dates established by the Subcommittee or, if applicable, the Extended Proceeding Committee, the National Adjudicatory Council, the Review Subcommittee, or Counsel to the National Adjudicatory Council in a scheduling order. Unless the Subcommittee or, if applicable, the Extended Proceeding Committee, the National Adjudicatory Council, the Review Subcommittee, or Counsel to the National Adjudicatory Council specifies otherwise, opening briefs shall be submitted not less than 21 days from the date of the scheduling order, and answering briefs shall be submitted 21 days thereafter. When reply briefs are submitted, such briefs shall be filed not later than ten days after service of the answering brief. Counsel to the National Adjudicatory Council may not shorten a period previously established for the filing of briefs except with the consent of the Parties. The time periods listed in this provision are only applicable to the filing of opening briefs, answering briefs, and reply briefs.

9349. National Adjudicatory Council Formal Considera-tion; Decision

(a) Decision of National Adjudicatory Council, Including Remand

In an appeal or review of a disciplinary proceeding governed by the Rule 9300 Series that is not withdrawn or dismissed prior to a decision on the merits, the National Adjudicatory Council, after considering all matters presented in the appeal or review and the written recommended decision of the Subcommittee or, if applicable, the Extended Proceeding Committee, may affirm, dismiss, modify or reverse the decision of the Hearing Panel or, if applicable, Extended Hearing Panel, with respect to each Respondent who has appealed or cross-appealed or is subject to a call for review. The National Adjudicatory Council may affirm, modify, reverse, increase, or reduce any sanction, or impose any other fitting sanction. Alternatively, the National Adjudicatory Council or the Review Subcommittee may remand the disciplinary proceeding with instructions. The National Adjudicatory Council shall prepare a proposed written decision pursuant to paragraph (b).

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

9350. Discretionary Review by NASD Board

9351. Discretionary Review by NASD Board

(a) Call for Review by Governor

A Governor may call a disciplinary proceeding for review by the NASD Board. [if the call for review is made within the period prescribed in paragraph (b).] The Governor should call a case for review as soon as practicable, but no later than the second NASD Board meeting following the receipt of the proposed National Adjudicatory Council decision by the NASD Board.

(b) [15 Day Period; Waiver

(1) A Governor shall make his or her call for review not later than the next meeting of the NASD Board that is at least 15 days after the date on which the NASD Board receives the proposed written decision of the National Adjudicatory Council.

(2) Waiver

By a unanimous vote of the NASD Board, the NASD Board may shorten the period in subparagraph (1) to less than 15 days. By an affirmative vote of the majority of the NASD Board then in office, the NASD Board may, during the 15 day period in subparagraph (1), vote to extend the period in subparagraph (1) to more than 15 days.]

[(c)] Review [at Next Meeting]

If a Governor calls a disciplinary proceeding for review [within the period prescribed in paragraph (b)], the NASD Board shall review the disciplinary proceeding as soon as practicable. [not later than the next meeting of the NASD Board]. The NASD Board may order the Parties (excluding any Respondent who did not appeal or cross-appeal, or as to whom the issues appealed or called for review do not apply) to file briefs in connection with the review proceedings pursuant to this Rule.

(c)[(d)] Decision of NASD Board, Including Remand

After review, the NASD Board may affirm, modify, or reverse the proposed written decision of the National Adjudicatory Council. The NASD Board may affirm, modify, reverse, increase, or reduce any sanction, or impose any other fitting sanction. Alternatively, the NASD Board may remand the disciplinary proceeding with instructions. The NASD Board shall prepare a written decision that includes all of the elements described in Rule 9349(b)(1) through (6). The NASD Board shall reach a decision as soon as practicable, but no later than the second Board meeting following the call for review.

(d)[(e)] Issuance of Decision After Expiration of Call for Review Period No change.

9360. Effectiveness of Sanctions

Unless otherwise provided in the decision issued under Rule 9349 or Rule 9351, a sanction (other than a bar or an expulsion) specified in a decision constituting final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1) shall become effective on a date to be determined by Association staff [30 days after the date of service of the decision constituting final disciplinary action]. A bar or an expulsion shall become effective upon service of the decision constituting final disciplinary action of the Association [for purposes of SEC Rule 19d-1(c)(1)], unless otherwise specified therein. The Association shall serve the decision on a Respondent by [overnight] courier, facsimile or other means reasonable likely to obtain prompt service when the sanction is a bar or an expulsion.

9400. LIMITATION PROCEDURES UNDER RULES 3130 AND 3131

9410. Procedures for Regulating Activities of a Member Experiencing Financial or Operational Difficulties

9412. Notice of Limitations

The Department of Member Regulation may issue a notice directing a member to limit its business activities if the Department of Member Regulation has reason to believe that any condition specified in Rule 3130 or

3131 exists. The notice shall specify the grounds on which such action is being taken, the nature of the limitations to be imposed, the effective date of the limitations, a fitting sanction that will be imposed if the member fails to comply with the limitations set forth in the notice, and the conditions for terminating such limitations. The effective date of the limitations 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 under Rule 9413. The Department of Member Regulation shall serve the notice by facsimile or overnight [commercial] courier.

9413. [Department of Member Regulation Consideration

(a) Request for Hearing

A member aggrieved by a notice issued under Rule 9412 may file a written request for a hearing before the Department of Member Regulation. The request shall state the specific grounds for withdrawing or modifying the limitations 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.

(b) Stay

A request for hearing shall stay the notice of limitations served under Rule 9412 unless the National Adjudicatory Council orders otherwise.

(c) Time of Hearing

If a member requests a hearing under paragraph (a), the Department of Member Regulation shall conduct a hearing within 14 days after service of the notice under Rule 9412. Not less than five business days before the hearing, the Department of Member Regulation shall provide written notice to the member of the location, date, and time of the hearing by facsimile or overnight commercial courier.

(d) Transmission of Documents

(1) Not less than five business days before the hearing, the Department of Member Regulation shall provide to the member by facsimile or overnight commercial courier all documents that were considered in imposing the limitations on business activities set forth in the notice served under Rule 9412, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon conclusion of any review by the Commission or the federal courts.

(2) Not less than five business days before the hearing, the Department of Member Regulation and the member shall exchange proposed exhibit and witness lists. The exhibit and witness lists shall be served by facsimile or by overnight commercial courier.

(e) Hearing and Rights of Member

The member shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence. The hearing shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Department of Member Regulation within a reasonable time determined by the Department of Member Regulation. Upon notice to the participants in the hearing, the Department of Member Regulation may order corrections to the transcript as requested or sua sponte.

(f) Record

The record shall consist of:

(1) the notice issued pursuant to Rule 9412;

(2) all documents transmitted to the member under Rule 9413(d);

(3) the request for hearing filed pursuant to Rule 9413(a);

(4) any other submissions by the member and the Department of Member Regulation at the hearing;

(5) any evidence considered at the hearing; and

(6) the transcript of the hearing and any corrections thereto.

(g) Custodian of the Record

The custodian of the record shall be the Department of Member Regulation.

(h) 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 decision becomes final or, if applicable, upon the conclusion of any review by the

Commission or the federal courts.

(i) Decision

Within seven days after the hearing, the Department of Member Regulation shall issue a written decision approving, modifying, or withdrawing the limitations specified in the notice. If the decision imposes limitations, the decision shall state the grounds for the limitations, the conditions for terminating such limitations, and provide for a fitting sanction to be imposed under Rule 9416 if the member fails to comply with the limitations. The Department of Member Regulation shall promptly serve the decision by facsimile or overnight commercial courier. The limitations imposed shall become effective upon service of the decision.

(j) Failure to Request Hearing

If a member does not request a hearing under paragraph (a), the limitations specified in the notice shall become effective on the date specified in the notice. Unless the National Adjudicatory Council calls the notice for review under Rule 9414(a)(2), the limitations specified in the notice shall remain in effect until the Department of Member Regulation reduces or removes the limitations pursuant to Rule 9417(b).]

[9414.] Hearing Panel Review [National Adjudicatory Council Review]

[(a) Initiation of a Review]

(a)[(1)] Request for a Hearing [Application by Member]

A member aggrieved by a notice [decision] issued under Rule 9412 [9413] may file a written request [application] for hearing [review by] before a Hearing Panel [the National Adjudicatory Council] with the Office of Hearing Officers. The request [application] shall state the specific grounds for withdrawing or modifying the limitations 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 review and whether oral argument is requested. The application shall be filed pursuant to Rules 9135, 9136, and 9137 within seven days after service of the decision.] The member may withdraw its request [application for review] at any time by filing a written notice with the Office of Hearing Officers [National Adjudicatory Council] pursuant to Rules 9135, 9136, and 9137.

[(2) Motion of National Adjudicatory Council

A decision issued under Rule 9413 shall subject to a call for review by any member of National Adjudicatory Council or the Review Subcommittee within 30 days after service of the decision. If a member that receives a notice under Rule 9412 does not request a hearing under Rule 9413, the notice shall be subject to a call for review by any member of the National Adjudicatory Council or the Review Subcommittee within 30 days after the effective date of the notice. If the National Adjudicatory Council or the Review Subcommittee calls a decision or notice for review, a written notice of review shall be served promptly on the member pursuant to Rules 9132 and 9134. The notice of review shall state the specific grounds for the review and whether an oral argument is ordered. If a decision is called for review by a member of the National Adjudicatory Council or the Review Subcommittee, the National Adjudicatory Council shall review the decision.]

(b) Appointment of Hearing Panel

The Chief Hearing Officer shall assign a Hearing Officer to preside over the matter, and appoint Panelists pursuant to Rule 9231 and 9232 to the Hearing Panel. As soon as practicable after assignment, the Chief Hearing Officer shall serve the Parties with notice of the Hearing Panel.

(c)[(3)] Stay

Unless otherwise ordered by the NASD Board Executive Committee [National Adjudicatory Council], 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.

(d)[(4)] Transmission of Documents [the Record]

(1) Not less than five business days before the hearing, the Department of Member Regulation shall provide to the member by facsimile or overnight courier all documents that were considered in imposing the limitations on business activities set forth in the notice served under Rule 9412, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon conclusion of any review by the Commission or the federal courts.

(2) Not less than five business days before the hearing, the Department of Member Regulation and the member shall exchange proposed exhibit and witness lists. The exhibit

and witness lists shall be served by facsimile or by overnight courier.

(e) Time of Hearing

If a member requests a hearing under paragraph (a), the a Hearing Panel shall conduct a hearing within 14 days after service of the notice under Rule 9412. Not less than five business days before the hearing, the Office of Hearing Officers shall provide written notice to the member of the location, date, and time of the hearing by facsimile or overnight courier.

(f) Hearing and Rights of Member

The member shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence. The hearing shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Office of Hearing Officers within a reasonable time determined by the Office of Hearing Officers. Upon notice to the participants in the hearing, the Department of Member Regulation may order corrections to the transcript as requested or sua sponte.

(g) Record

The record shall consist of:

(1) the notice issued pursuant to Rule 9412;

(2) all documents transmitted to the member under Rule 9413;

(3) the request for hearing filed pursuant to Rule 9413;

(4) any other submissions by the member and the Department of Member Regulation at the hearing;

(5) any evidence considered at the hearing; and

(6) the transcript of the hearing and any corrections thereto.

(h) Custodian of the Record

The custodian of the record shall be the Office of Hearing Officers.

(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 decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

[If a review is initiated under this paragraph, the Department of Member Regulation shall assemble and prepare an index of the record, transmit the record and index to the National Adjudicatory Council, certify to the National Adjudicatory Council that the record is complete, and serve a copy of the record and index on the member.]

(j) Failure to Request Hearing

If a member does not request a hearing under paragraph (a), the limitations 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 specified in the notice shall remain in effect until a Hearing Panel reduces or removes the limitations pursuant to Rule 9417(b).

(k) Decision

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

(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 become final, and the Hearing Pane shall 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.

(m)[(5)] Ex Parte Communications

The prohibitions against ex parte communications in Rule 9143 shall become effective under the Rule 9410 Series when Association staff has knowledge that a member intends to file a written application for review or that the NASD Board Executive Committee [National Adjudicatory Council] intends to review a decision on its own motion under this Rule.

[(b) Subcommittee Consideration

(1) Appointment of Subcommittee

The National Adjudicatory Council or the Review Subcommittee shall appoint a Subcommittee to participate in the review. The Subcommittee shall be composed of two or more members. One member shall be a member of the National Adjudicatory Council, and the remaining member or members shall be current or former members of the National Adjudicatory Council or a former Director or Governor.

(2) Oral Argument

If oral argument is timely requested by the member, oral argument shall be held before the Subcommittee within 14 days after service of the decision under Rule 9413. If oral argument is ordered by the Subcommittee, oral argument shall be held before the Subcommittee within 14 days after service of the order under paragraph (a)(2). The member shall be entitled to be represented by an attorney. The oral argument shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Subcommittee within a reasonable time determined by the Subcommittee. Upon notice to the participants in the hearing, the Subcommittee may order corrections to the transcript as requested or sua sponte.

(3) Review on Record

The Subcommittee shall conduct its review on the basis of the record, any written submissions by the member and the Department of Member Regulation, and the decision issued pursuant to Rule 9413(i). If oral argument is requested or ordered, Subcommittee also may consider any submissions or additional arguments by the member and the Department of Member Regulation.

(4) Additional Evidence

The Subcommittee may consider any additional relevant and material evidence if the member shows good cause for not previously submitting such evidence. If additional evidence is accepted by the Subcommittee, the evidence shall be included in the record. Proffered evidence that is not accepted into the record by the Subcommittee shall be retained until the date when the Association's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

(5) Recommendation

The Subcommittee shall present a recommended decision in writing to the National Adjudicatory Council not later than seven days before the meeting of the National Adjudicatory Council at which the proceeding shall be considered.

(c) Decision

(1) Decision of National Adjudicatory Council, Including Remand

After considering all matters presented in the review and the written recommended decision of the Subcommittee, the National Adjudicatory Council] may affirm, modify, or reverse the Department of Member Regulation's decision or remand the proceeding with instructions. The National Adjudicatory Council shall prepare a proposed written decision pursuant to subparagraph (2).

(2) Contents of Decision

The decision shall include:

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

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

(C) a summary of the evidence on each issue;

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

(E) if any limitations are imposed:

(i) a description of the limitations 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; and

(ii) the conditions for terminating the limitations.

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

The National Adjudicatory Council shall provide its proposed written decision to the NASD Board. The NASD Board may call the proceeding for review pursuant to Rule 9415. If the NASD Board does not call the proceeding for review, the proposed written decision of National Adjudicatory Council shall become final, and the National Adjudicatory Council shall 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, unless National Adjudicatory Council remands the proceeding.]

9415. Discretionary Review by the NASD Board Executive Committee

(a) Call for Review by NASD Board Executive Committee [Governor]

A member of the NASD Board Executive Committee [Governor] may call a proceeding for review by the NASD Board Executive Committee if the call for review is made within the period prescribed in paragraph (b).

(b) 15 Day Period; Waiver

A member of the NASD Board Executive Committee [Governor] shall make his or her call for review not later than the next meeting of the NASD Board Executive Committee that is at least 15 days after the date on which the NASD Board Executive Committee receives the proposed written decision of the Hearing Panel [National Adjudicatory Council]. By a unanimous vote of the NASD Board Executive Committee, the NASD Board Executive Committee may shorten the period to less than 15 days. By an affirmative vote of the majority of the NASD Board Executive Committee then in office, the NASD Board Executive Committee may, during the 15 day period, vote to extend the period to more than 15 days.

(c) Review at Next Meeting

If an NASD Board Executive Committee member [Governor] calls a proceeding for review within the period prescribed in paragraph (b), the NASD Board Executive Committee shall review the proceeding not later than the next meeting of the NASD Board Executive Committee. The NASD Board Executive Committee may order the filing of briefs in connection with its review proceedings pursuant to this Rule.

(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 [National Adjudicatory Council]. Alternatively, the NASD Regulation Board 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)[(c)(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, 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 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 [commercial] courier.

(b) Hearing

(1) A member aggrieved by an order issued under paragraph (a) may file a written request for a hearing before a Hearing Panel with the Office of Hearing Officers [the Department of Member Regulation]. The request shall be filed pursuant to Rules 9135, 9136, and 9137 within seven days (including intermediate Saturdays, Sundays, and Federal holidays) after service of the order. The Chief Hearing Officer shall assign a Hearing Officer to preside over the matter, and appoint Panelists pursuant to Rule 9231 and 9232 to the Hearing Panel. As soon as practicable after assignment, the Office of Hearing Officers shall serve the Parties with notice of the Hearing Panel. The hearing shall be held within ten days after service of the order under paragraph (a).

(2) The member shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence.

(3) The hearing shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Office of Hearing Officers [Department of Member Regulation] within a reasonable time determined by the Office of Hearing Officers [Department of Member Regulation]. Upon notice to the participants in the hearing, the Office of Hearing Officers [Department of Member Regulation] may order corrections to the transcript as requested or sua sponte.

(c) No Stay of Sanctions

Unless otherwise ordered by the NASD Board Executive Committee [National Adjudicatory Council], a request for a hearing pursuant to this Rule shall not stay the effectiveness of the order issued under paragraph (a).

(d) Decision

Within four days after the hearing, the Hearing Panel [Department of Member Regulation] shall affirm, modify, or reverse the order issued under paragraph (a). The Office of Hearing Officers [Department of Member Regulation] 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.

9500. OTHER PROCEEDINGS

9510. Summary and Non-Summary Proceedings

9512. Initiation of Summary Proceeding

(a) Authorization No change.

(b) Contents and Service of Notice

A notice issued under this subsection shall state the specific grounds and include the factual basis for the summary suspension, limitation, or prohibition and state that the member, associated person, or other person may file a written request for a hearing under Rule 9514. The notice shall be served by facsimile or overnight [commercial] courier.

(c) Effective Date No change.

9513. Initiation of Non-Summary Proceeding

(a) Notice

Association staff may initiate a proceeding authorized under Rule 9511(a)(2)(A) or (B), by issuing a written notice to the member, associated person, or other person. The notice shall specify the grounds for and effective date of the cancellation, suspension, bar, limitation, or prohibition and shall state that the member, associated person, or other person may file a written request for a hearing under Rule 9514. The notice shall be served by facsimile or overnight [commercial] courier.

(b) Effective Date No change.

9514. Hearing and Decision

(a) Request

(1) Request by Member, Associated Person, or Other Person

No change.

(2) Failure to File Request

If the member, associated person, or other person subject to the notice issued under Rule 2210, 2220, 9512(a), or 9513(a) does not file a written request for a hearing within the seven day time period specified in [under] subparagraph (1), the notice shall constitute final action by the Association.

(3) Ex Parte Communications No change.

(b) Designation of Party for the Association and Appointment of Hearing Panel

If a member, associated person, or other person subject to a notice under Rule 2210, 2220, 9512, or 9513 files a written request for a hearing, an appropriate department or office of the Association shall be designated as a Party in the proceeding, and a Hearing Panel shall be appointed.

(1) through (2) No change.

(3) A Hearing Officer appointed pursuant to this provision shall have authority to do all things necessary and appropriate to discharge his or her duties as set forth under Rule 9235.

(c) Stays No change.

(d) Time of Hearing

(1) Summary Proceeding

If a member, associated person, or other person who is subject to a notice issued under Rule 9512(a) files a written request for a hearing, a hearing shall be held within seven days after the filing of the request for hearing. Not less than five days before the hearing, the Hearing Panel shall provide written notice to the Parties of the location, date,

and time of the hearing by facsimile or overnight [commercial] courier.

(2) Non-Summary Proceeding

If a member, associated person, or other person who is subject to a notice issued under Rule 2210, 2220, or 9513(a) files a written request for a hearing, a hearing shall be held within 40 [21] days after the filing of the request for hearing. The Hearing Panel may, during the initial 40 [21] day period, extend the time in which the hearing shall be held by an additional 30 [21] days on its own motion or at the request of a Party. Not less than five days before the hearing, the Hearing Panel shall provide written notice to the Parties of the location, date, and time of the hearing by facsimile or overnight [commercial] courier.

(e) Transmission of Documents

(1) Not less than five days before the hearing, the Association shall provide to the member, associated person, or other person who requested the hearing, by facsimile or overnight [commercial] courier, all documents that were considered in issuing the notice under Rule 2210, 2220, 9512, or 9513, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

(2) Not less than five days before the hearing, the Parties shall exchange proposed exhibit and witness lists. The exhibit and witness lists shall be served by facsimile or by overnight [commercial] courier.

(f) Hearing Panel Consideration
No change.

9516. Reinstatement

A member, associated person, or other person who has been suspended or limited by a final action of the Association under the Rule 9510 Series may file a written request for reinstatement on the ground of full compliance with the conditions of the suspension or limitation. The request shall be filed with the department or office of the Association that acted as a Party in the proceeding. The head of the department or office shall serve its response on the member or person via facsimile or overnight [commercial] courier within five days after receipt of the request. If the head of the department or office denies the request, the member or person may file a written request for relief with the Review Subcommittee [NASD Board]. The Review Subcommittee [NASD Board] shall respond to the request in writing within 14 days after receipt of the request. The Review Subcommittee [NASD Board] shall serve its response by facsimile or overnight [commercial] courier.

9520. Eligibility Proceedings

9521. Purpose and Definitions

(a) Purpose

The Rule 9520 Series sets forth procedures for a person to become or remain associated with a member, notwithstanding the existence of a [statutory] disqualification as defined in Article III, Section 4 of the NASD By-Laws [Section 3(a)(39) of the Act] and for a current member or person associated with a member to obtain relief from the eligibility or qualification requirements of the NASD By-Laws and the Rules of Association. Such actions hereinafter are referred to as "eligibility proceedings."

(b) Definitions

(1) The term "application" means NASD Regulation's Form MC-400 for individuals or Form MC-400A for members, filed with the Central Registration Depository/Public Disclosure.

(2) The term "disqualified member" means a broker, dealer, municipal securities broker or dealer, government securities broker or dealer, or member that is or becomes subject to a disqualification or is otherwise ineligible for membership under Article III, Section 3 of the NASD's By-Laws.

(3) The term "disqualified person" means an associated person or person seeking to become an associated person who is or becomes subject to a disqualification or is otherwise ineligible for association under Article III, Section 4 of the NASD's By-Laws.

(4) The term "sponsoring member" means the member or applicant for membership pursuant to Rule 1013 that is sponsoring the association or continued association of a disqualified person to be admitted, readmitted, or permitted to continue in association.

9522. Initiation of Eligibility Proceeding; Member Regulation Consideration

(a) Initiation by Association

(1) Issuance of Notice of Disqualification or Ineligibility

If Association staff has reason to believe that a [statutory] disqualification exists or that a member or person associated with a member otherwise fails to meet the eligibility requirements of the Association, Association staff shall issue a written notice to the member or applicant for membership under Rule 1013 [associated person]. The notice shall specify the grounds for such disqualification or ineligibility.

(2) Notice Regarding a [to] Member

A notice issued to a disqualified member [that is subject to a statutory disqualification or is otherwise ineligible for membership] shall state that the disqualified member may apply for relief by filing an [written] application [for relief pursuant to paragraph (c) with the National Adjudicatory Council] or, in the case of a matter set forth in Rule 9522(e)(1), a written request for relief, within ten business days after service of the notice. If the member fails to file the [written] application [for relief] or, where appropriate, the written request for relief, within the 10-day period, the membership of the member shall be canceled, unless the Department of Member Regulation grants an extension for good cause shown.

(3) Notice Regarding an [to] Associated Person

A notice issued [to] regarding a[n] [associated] disqualified person [who is subject to a statutory disqualification or is otherwise ineligible for association] to a member or applicant for membership under Rule 1013 shall state that [a] such member or applicant for membership may file an application [apply for relief] on behalf of itself and such person [by filing a written application for relief pursuant to paragraph (c) with the National Adjudicatory Council] or, in the case of a matter set forth in Rule 9522(e)(1), a written request for relief, within ten business days after service of the notice. If the member fails to file the [written] application [for relief] or, where appropriate, the written request for relief, within the 10-day period, the registration of the [associated] disqualified person shall be revoked, unless the Department of Member Regulation grants an extension for good cause shown.

(4) Service

A notice issued under this section shall be served by facsimile or pursuant to Rules 9131 and 9134.

(b) Obligation of Member to Initiate Proceeding

A member shall file an [written] application [for relief from the eligibility requirements of the Association pursuant to paragraph (c) with the National Adjudicatory Council] or, in the case of a matter set forth in Rule 9522(e)(1), a written request for relief, with the Central Registration Depository/ Public Disclosure, if the member determines prior to receiving a notice under paragraph (a) that:

(1) it has become a disqualified member [the member is subject to a statutory disqualification or otherwise is no longer eligible for membership];

(2) a person associated with such member or whose association is proposed by an applicant for membership under Rule 1013 has become a disqualified person [is subject to a statutory disqualification or otherwise is no longer eligible for association with the member]; or

(3) the member or applicant for membership under Rule 1013 wishes to sponsor the association of a person who is a disqualified person. [subject to a statutory disqualification or otherwise is ineligible for association with a member.]

[(c) Form of Application for Relief]

[A written application for relief shall be submitted on Form MC-400 and shall include a detailed statement demonstrating why the requested relief should be granted.]

(c)[(d)] Withdrawal of Application

A member may withdraw its application or written request for relief prior to a hearing [at any time] by filing a written notice with the [National Adjudicatory Council] Central Registration Depository/Public Disclosure pursuant to Rules 9135, 9136, and 9137. A member may withdraw its application after the start of a hearing but prior to the issuance of a decision by the National Adjudicatory Council with prior written consent of the National Adjudicatory Council.

(d)[(e)] Ex Parte Communications

The prohibitions against ex parte communications set forth in Rule 9143 shall become effective under the Rule 9520 Series when Association staff has initiated the eligibility proceeding and Association staff has knowledge that a member intends to file an [written] application or written request for relief pursuant to the

Rule 9520 Series [with the National Adjudicatory Council].

(e) Member Regulation Consideration

(1) Matters that may be Approved by the Department of Member Regulation without the Filing of an Application

The Department of Member Regulation, as it deems consistent with the public interest and the protection of investors, may grant a written request for relief from the eligibility requirements by a disqualified member or a sponsoring member without the filing of an application by such disqualified member or sponsoring member if a disqualified member or disqualified person is subject to one or more of the following conditions but is not otherwise subject to disqualification:

(A) a disqualified member or disqualified person is subject to a disqualification based on an injunction that was entered ten or more years prior to the proposed admission or continuance by order, judgment, or decree of any court of competent jurisdiction from acting as an investment adviser, underwriter, broker, dealer, municipal securities dealer, government securities broker, government securities dealer, transfer agent, foreign person performing a function substantially equivalent to any of the above, entity or person required to be registered under the Commodity Exchange Act, or any substantially equivalent foreign statute or regulation, or as an affiliated person or employee of any investment company, bank, insurance company, foreign entity substantially equivalent to any of the above, or entity or person required to be registered under the Commodity Exchange Act or any substantially equivalent foreign statute or regulation, or from engaging in or continuing any conduct or practice in connection with any such activity, or in connection with the purchase or sale of any security.

(B) a sponsoring member makes a request to change the supervisor of a disqualified person; or

(C) a disqualified member or sponsoring member is a member of both the Association and another self-regulatory organization; and:

(i) the other self-regulatory organization intends to file a Notice under SEC Rule 19h-1 approving the membership continuance of the disqualified member or, in the case of a sponsoring member, the proposed association or continued association of the disqualified person; and

(ii) Member Regulation concurs with that determination.

(2) Matters that may be Approved by the Department of Member Regulation after the Filing of an Application

The Department of Member Regulation, as it deems consistent with the public interest and the protection of investors, may approve an application filed by a disqualified member or sponsoring member if a disqualified member or disqualified person is subject to one or more of the following conditions but is not otherwise subject to disqualification (other than a matter set forth in subparagraph(e)(1)):

(A) The disqualified person is already a participant in, a member of, or a person associated with a member of, a self-regulatory organization, and the terms and conditions of the proposed admission are the same in all material respects as those imposed or not disapproved in connection with such person's prior admission or continuance pursuant to an order of the Commission under SEC Rule 19h-1 or other substantially equivalent written communication;

(B) The Department of Member Regulation finds, after reasonable inquiry, that except for the identity of the employer concerned, the terms and conditions of the proposed admission or continuance are the same in all material respects as those imposed or not disapproved in connection with a prior admission or continuance of the disqualified person pursuant to an order of the Commission under SEC Rule 19h-1 or other substantially equivalent written communication, and that there is no intervening conduct or other circumstance that would cause the employment to be inconsistent with the public interest or the protection of investors; or

(C) The disqualification previously was a basis for the institution of an administrative proceeding pursuant to a provision of the federal securities laws, and was considered by the Commission in determining a sanction

against such disqualified person in the proceeding; and the Commission concluded in such proceeding that it would not restrict or limit the future securities activities of such disqualified person in the capacity now proposed, or, if it imposed any such restrictions or limitations for a specified time period, such time period has elapsed.

(3) Rights of Disqualified Member, Sponsoring Member, Disqualified Person, and Department of Member Regulation

(A) In the event the Department of Member Regulation does not approve a written request for relief from the eligibility requirements pursuant to subparagraph (e)(1), the disqualified member or sponsoring member may file an application, and such member shall have the right to proceed under Rule 9523 or 9524, as applicable. The Department of Member Regulation may require a disqualified member or sponsoring member to file an application with the Central Registration Depository/Public Disclosure, notwithstanding the provisions of subparagraph (e)(1).

(B) In the event the Department of Member Regulation does not approve an application pursuant to subparagraph (e)(2), the disqualified member or sponsoring member shall have the right to proceed under Rule 9523 or 9524, as applicable.

9523. Acceptance of Member Regulation Recommendations and Supervisory Plans by Consent Pursuant to SEC Rule 19h-1

(a) After an application is filed, the Department of Member Regulation may recommend the membership or continued membership of a disqualified member or sponsoring member or the association or continuing association of a disqualified person pursuant to a supervisory plan where the disqualified member, sponsoring member, and/or disqualified person, as the case may be, consent to the recommendation and the imposition of the supervisory plan. The disqualified member, sponsoring member, and/or disqualified person, as the case may be, shall execute a letter consenting to the imposition of the supervisory plan.

(b)(1) If a disqualified member, sponsoring member, and/or disqualified person submit an executed letter consenting to a supervisory plan, by the submission of such letter, the disqualified member, sponsoring member and/or disqualified person waive:

(A) the right to a hearing before a Hearing Panel and any right of appeal to the National Adjudicatory Council, the Commission, and the courts, or otherwise challenge the validity of the supervisory plan, if the supervisory plan is accepted.

(B) any right of the disqualified member, sponsoring member, and/or disqualified person to claim bias or prejudgment by the Department of Member Regulation, the General Counsel, the National Adjudicatory Council, or any member of the National Adjudicatory Council, in connection with such person's or body's participation in discussions regarding the terms and conditions of the Department of Member Regulation's recommendation or the supervisory plan, or other consideration of the recommendation or supervisory plan, including acceptance or rejection of such recommendation or supervisory plan; and

(C) any right of the disqualified member, sponsoring member, and/or disqualified person to claim that a person violated the *ex parte* prohibitions of Rule 9143 or the separation of functions prohibitions of Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of the recommendation or supervisory plan, or other consideration of the recommendation or supervisory plan, including acceptance or rejection of such recommendation or supervisory plan.

(2) If a recommendation or supervisory plan is rejected, the disqualified member, sponsoring member, and/or disqualified person shall be bound by the waivers made under subparagraph (b)(1) for conduct by persons or bodies occurring during the period beginning on the date the supervisory plan was submitted and ending upon the rejection of the supervisory plan and shall have the right to proceed under this rule and Rule 9524, as applicable.

(c) If the disqualified member, sponsoring member, and/or disqualified person execute the letter consenting to the supervisory plan, it shall be submitted to the General Counsel and/or the Chairman of the Statutory Disqualification Committee, acting on behalf of the National Adjudicatory Council, by the Department of Member Regulation

with a proposed Notice under SEC Rule 19h-1, where required. The Chairman of the Statutory Disqualification Committee or the General Counsel may accept the recommendation of the Department of Member Regulation and the supervisory plan or refer them to the National Adjudicatory Council for acceptance or rejection by the National Adjudicatory Council. The Chairman of the Statutory Disqualification Committee may reject such recommendation and supervisory plan or refer them to the National Adjudicatory Council for acceptance or rejection by the National Adjudicatory Council.

(d) If the recommendation and supervisory plan is accepted by the National Adjudicatory Council, the Chairman of the Statutory Disqualification Committee, or the General Counsel, it shall be deemed final and, where required, the proposed Notice under SEC Rule 19h-1 will be filed by the Association. If the recommendation and supervisory plan are rejected by the Chairman of the Statutory Disqualification Committee or the National Adjudicatory Council, NASD Regulation may take any other appropriate action with respect to the disqualified member, sponsoring member, and/or disqualified person. If the recommendation and supervisory plan are rejected, the disqualified member, sponsoring member, and/or disqualified person shall not be prejudiced by the execution of the letter consenting to the supervisory plan under subparagraph (a) and the letter may not be introduced into evidence in any proceeding.

9524[9523]. National Adjudicatory Council Consideration

(a) Hearing Panel Consideration

(1) Appointment of Hearing Panel

When a hearing is necessary under this Series [If a member files an application for relief], the National Adjudicatory Council or the Review Subcommittee shall appoint a Hearing Panel composed of two or more members, who shall be current or former members of the National Adjudicatory Council or the Statutory Disqualification Committee or former Directors or Governors. The Hearing Panel shall conduct a hearing and recommend a decision on the request for relief.

(2) Notice of Hearing

The disqualified member or sponsoring member, as the case may be, and the Department of Member Regulation [Not less than fourteen days before the hearing, the member] shall be notified via mail, facsimile, or overnight [commercial] courier of the location, time, and date of the hearing not less than fourteen business days before the hearing, unless the parties agree to shorten the time period.

(3) Transmission of Documents

(A) Upon receipt of an application, the Central Registration Depository shall gather all of the information necessary to process the application, including (i) the Central Registration Depository records for the disqualified member, sponsoring member, and/or disqualified person, as the case may be, and the proposed supervisor; and (ii) all of the information submitted by the disqualified member or sponsoring member in support of the application. The Central Registration Depository will prepare an index of these documents, and simultaneously provide this index and copies of the documents to the disqualified member or sponsoring member, as the case may be, the Office of the General Counsel, and the Department of Member Regulation. [If Association staff initiated the eligibility proceeding by issuing a notice under Rule 9522(a), Association staff shall provide to the member and its current or prospective associated person all documents that were relied on in issuing the notice.] Such documents shall be served on the disqualified member [and its current or prospective associated person] or sponsoring member, as the case may be, by mail, facsimile, or overnight [commercial] courier as soon as practicable [not less than ten days before the hearing]. The Department of Member Regulation shall serve its recommendation and its supporting documents on the Hearing Panel and the disqualified member or sponsoring member, as the case may be, within ten business days of the hearing, unless the Parties agree otherwise. The disqualified member or sponsoring member, as the case may be, shall serve its documents on the Hearing Panel and the Department of Member Regulation within ten business days of the hearing, unless the Parties agree otherwise.

(B) Not less than ten business days before the hearing, the Department of Member Regulation, which shall act as a Party in the eligibility proceeding, and the disqualified member [and its current or prospective associated person] or sponsoring member, as the

case may be, shall [exchange] serve proposed exhibit and witness lists on each other and the Hearing Panel. [The exhibit and witness lists shall be served by facsimile or overnight [commercial] courier.]

(C) At any time prior to the issuance of its recommendation, the Hearing Panel may order the Parties to supplement the record with any additional information that the Hearing Panel deems necessary.

(4) Rights of Disqualified Member, Sponsoring Member, Disqualified [Current or Prospective Associated] Person, and Department of Member Regulation

The disqualified member, sponsoring member, [its current or prospective associated] and/or disqualified person, as the case may be, and, the Department of Member Regulation, shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence.

(5) Extensions of Time, Postponements, and Adjournments

At any time prior to the issuance of the decision of the Hearing Panel, after obtaining consent of all the Parties, the Hearing Panel may extend or shorten any time limits prescribed by the Code for the filing of any papers and may postpone or adjourn any hearing.

(6)[(5)] Recordation of Hearing

The hearing shall be recorded and a transcript prepared by a court reporter. The disqualified member, sponsoring member, and/or [the current or prospective associated] disqualified person, as the case may be, may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Hearing Panel within a reasonable time determined by the Hearing Panel. Upon notice to the participants in the hearing, the Hearing Panel may order corrections to the transcript as requested or sua sponte.

(7)[(6)] Record

The record shall consist of:

(A) the notice issued pursuant to Rule 9522(a), if applicable;

(B) all documents relied upon in issuing the notice under Rule 9522(a), if applicable;

(C) the application for relief filed pursuant to Rule 9522(b);

(D) any other submissions by the disqualified member, sponsoring member, and/or [the] [current or prospective associated] disqualified person, as the case may be, and the Department of Member Regulation;

(E) any evidence considered at the hearing; and

(F) the transcript of the hearing and any corrections thereto.

(8)[(7)] Custodian of the Record

The custodian of the record shall be the Office of General Counsel of NASD Regulation.

(9)[(8)] 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 decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

(10)[(9)] Recommendation

On the basis of the record, the Hearing Panel shall present a recommended decision in writing on the request for relief to the Statutory Disqualification Committee. After considering the record and recommendation of the Hearing Panel, the Statutory Disqualification Committee shall present its recommended decision in writing to the National Adjudicatory Council [not later than seven days before the meeting of the National Adjudicatory Council at which the eligibility proceeding shall be considered].

(b) Decision

(1) Decision of the National Adjudicatory Council

After considering all matters presented in the request for relief, the Statutory Disqualification Committee's recommended decision, the public interest, and the protection of investors, the National Adjudicatory Council may grant or deny the request for relief, and, if relief is granted, impose conditions on the disqualified member, sponsoring member, and/or [its current or prospective associated] disqualified person, as the case may be. At any time prior to the

issuance of its recommendation, the National Adjudicatory Council may order the Parties to supplement the record with any additional information that the National Adjudicatory Council deems necessary. Alternatively, the National Adjudicatory Council may remand the eligibility proceeding. The National Adjudicatory Council shall prepare a proposed written decision pursuant to subparagraph (2).

(2) Contents of Decision

The decision shall include:

(A) No change.

(B) No change.

(C) a statement in support of the disposition of the request for relief, which, if granted, includes any of the applicable elements under SEC Rule 19h-1(e) and a description of any conditions that are imposed on the disqualified member, sponsoring member, or disqualified [and current or prospective associated] person, as the case may be.

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

The National Adjudicatory Council shall provide its proposed written decision to the NASD Board. The NASD Board may call the eligibility proceeding for review pursuant to Rule 9525 [9524]. If the NASD Board does not call the eligibility proceeding for review, the proposed written decision of the National Adjudicatory Council shall become final, and the National Adjudicatory Council shall serve its written decision on the disqualified member, sponsoring member, and/or [the current or prospective associated] disqualified person, as the case may be, and the Department of Member Regulation pursuant to Rules 9132 and 9134. [The decision shall be effective upon service.] The decision shall constitute final action of the Association, unless the National Adjudicatory Council remands the eligibility proceeding. The decision shall be effective upon approval by the Commission.

9525[9524]. Discretionary Review by the NASD Board

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

(d) Decision of NASD Board, Including Remand

After review, the NASD Board may affirm, modify, or reverse the proposed written decision of the National Adjudicatory Council. Alternatively, the NASD Board may remand the eligibility proceeding with instructions. The NASD Board shall prepare a written decision that includes all of the elements described in Rule 9524(b)(2) [9523(b)(2)].

(e) Issuance of Decision

The NASD Board shall issue and serve its written decision on the disqualified member, sponsoring member, and/or disqualified [the current or prospective associated] person, as the case may be, 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, unless the NASD Board remands the proceeding. The decision shall be effective upon approval by the Commission.

9526[9525]. Expedited Review

(a) Direction by Executive Committee

Notwithstanding Rules [9523 and] 9524 and 9525, the NASD Board Executive Committee, upon request of the Statutory Disqualification Committee, may direct an expedited review of a recommended written decision of the Statutory Disqualification Committee if the NASD Board Executive Committee determines that expedited review is necessary for the protection of investors.

(b) Call for Review Period No change.

(c) No Call for Review

If no Governor calls the proceeding for review within the time prescribed, the decision shall become final, and the Statutory Disqualification Committee shall serve the decision on the disqualified member, sponsoring member, and/or disqualified [the current or prospective associated] person, as the case may be, and the Department of Member Regulation pursuant to Rules 9132 and 9134. The decision shall [be effective upon service and shall] constitute final action of the Association. The decision shall be effective upon approval by the Commission.

(d) Call for Review

If a Governor calls the eligibility proceeding for review within the prescribed time, a review panel shall meet and conduct a review not later than 14 days after the call for review. The review panel shall be composed of the NASD Board Executive Committee, except that the Governor who calls the proceeding for review shall serve on the review panel in lieu of a

member of the Executive Committee who has the same classification (Industry, Non-Industry, or Public) as such Governor. The review panel may affirm, modify, or reverse the recommended written decision of the Statutory Disqualification Committee or remand the eligibility proceeding with instructions. The review panel shall prepare, issue, and serve its decision pursuant to Rule [9524] 9525(d) and (e).

9527[9526]. Application to Commission for Review

The right to have any action taken 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 final action by the Association, unless the Commission otherwise orders.]

9530. Suspension or Cancellation for Failure to Pay Dues, Fees and Other Charges

9531. Notice

(a) Notice No change.

(b) Service of Notice

Association staff shall serve the notice via personal service, [by] facsimile or overnight [commercial] courier and shall file a copy of the notice with the Office of Hearing Officers.

(c) Effective Date of Notice No change.

9532. Hearing

(a) Request for Hearing No change.

(b) Hearing Procedures

(1) through **(3)** No change.

(4) Transmission of Documents

Not later than seven days before the hearing, the NASD Treasurer shall serve the member or person associated with a member via overnight [commercial] courier with all documents that were considered in connection with the decision to issue a notice under Rule 9531 and provide copies of the same to the Hearing Officer.

(5) through **(11)** No change.

9535. Termination of Suspension

A suspended member or person may file a written request for termination of the suspension on the ground of full compliance with the notice issued under Rule 9531 or, if applicable, the conditions of a decision under Rule 9533, with the Office of Hearing Officers. The Office of Hearing Officers shall respond to the request in writing within five days after receipt of the request. The Office of Hearing Officers shall send the written response via overnight [commercial] courier or facsimile.

9540. Failure to Provide Information or Meet the Eligibility and Qualification Standards

9541. Notice

(a) Notice to Member for Failure to Provide Information

If a member fails to provide any information, report, material, data, or testimony requested or required to be filed pursuant to the NASD By-Laws or the Rules of the Association, or fails to keep its membership application or supporting documents current, the Association staff may provide written notice to such member specifying the nature of the failure and stating that the failure to take corrective action within 20 days after service of the notice constitutes grounds for suspension of membership.

(b) Notice to Person Associated with Member for Failure to Provide Information

If a person associated with a member fails to provide any information, report, material, data, or testimony requested or required to be filed pursuant to the NASD By-Laws or the Rules of the Association, the Association staff may provide written notice to such person specifying the nature of the failure and stating that the failure to take corrective action within 20 days after service of the notice constitutes grounds for suspending the association of the person with the member.

(c) Notice to Member for Failure to Meet the Eligibility and Qualification Standards

If a member becomes ineligible for continuance in membership because it does not meet the eligibility and qualification standards set forth in Article III of the By-Laws, the Association staff may provide written notice to such member stating that the failure to become eligible for continuance in membership within 20 days after service of the notice constitutes grounds for cancellation of membership.

(d) Service of Notice

The Association staff shall serve the member or person associated with a member with such notice via personal service or overnight courier or by facsimile at location described in Rule 9134(b). Service by overnight courier shall be accomplished by sending the papers through an overnight courier service that generates a written confirmation of receipt or of attempts at delivery.

(e) Effective Date of Notice

A notice issued and served under this Rule shall becomes effective 20 days after the date of service of the notice.

9542. Hearing

(a) Request for Hearing

Within five days after the date of service of a notice issued under Rule 9541, the member or person served with such notice may file with the Office of Hearing Officers a written request for a hearing. The request shall state with specificity why the member or person believes that the notice should be set aside. The request for the hearing shall stay the effective date of the notice.

(b) Hearing Procedures

(1) Appointment of Hearing Panel

If a hearing is requested, based upon a notice issued under Rule 9541(a) or (b), the Chief Hearing Officer shall assign a Hearing Officer to preside over the matter, and appoint Panelists pursuant to Rules 9231 and 9232 to the Hearing Panel. As soon as practicable after the assignment, the Chief Hearing Officer shall serve the Parties with notice of the Hearing Panel.

(2) Appointment of a Hearing Officer

If a hearing is requested, based upon a notice issued under Rule 9541(c), the Chief Hearing Officer shall assign a Hearing Officer to conduct the hearing and decide whether the member should be canceled. As soon as practicable after the assignment, the Chief Hearing Officer shall serve the Parties with notice of the Hearing Officer.

(3) Parties

The Parties shall be the member or person to whom the notice was issued and the head of the department or office that issued the notice under Rule 9541.

(4) Time of Hearing

The hearing shall be held within 45 days after the date of service of the notice under Rule 9541. Not later than seven days before the hearing, the Hearing Officer shall serve the Parties with written notice of the date and time of the hearing.

(5) Transmission of Documents

Not later than seven days before the hearing, the head of the department or office that issued the notice under Rule 9541 shall serve the member or person associated with a member via overnight courier with all documents that were considered in connection with the decision to issue a notice under Rule 9541 and provide copies of the same to the Hearing Officer.

(6) Counsel

The Parties may be represented by counsel at a hearing conducted under this Rule.

(7) Evidence

Formal rules of evidence shall not apply to a hearing under this Rule. Not later than four days before the hearing, the Parties shall exchange copies of proposed hearing exhibits and witness lists and provide copies of the same to the Hearing Officer.

(8) Witnesses

A person who is subject to the jurisdiction of the Association shall testify under oath or affirmation. The oath or affirmation shall be administered by a court reporter or a notary public.

(9) Additional Information

At any time during its consideration, the Hearing Officer may direct the Parties to submit additional information. Any additional information submitted shall be provided promptly to all Parties at least one business day before the Hearing Panel renders its decision.

(10) Transcript

The hearing shall be recorded and a transcript prepared by a court reporter. A Party may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Hearing Officer within a reasonable time determined by the Hearing Officer. Upon notice to the participants in the hearing, the Hearing Officer may order corrections to the transcript as requested or sua sponte.

(11) Record

The record shall consist of all documents that were considered in connection with the decision to issue a notice under Rule 9541, the notice issued under Rule 9541, the request for hearing filed under Rule 9542, the transcript of the hearing, and each document or other item of evidence presented to or considered by the Hearing

Panel renders its decision. The Office of Hearing Officers shall be the custodian of the record.

(12) Failure to Appear at Hearing

If a member or person fails to appear at a hearing for which he has notice, the Hearing Officer may dismiss the request for a hearing as abandoned, and the notice issued under Rule 9541 shall become final. Upon a showing of good cause, the Hearing Officer may withdraw a dismissal entered pursuant to this subparagraph.

9543. Decision

(a) Failure to Provide Information

The Hearing Panel may impose any fitting sanction, including fines, suspension, expulsions and bars, based upon the failure to provide any information, report, material, data, or testimony requested or required to be filed pursuant to the NASD By-Laws or the Rules of the Association, or failure to keep a membership application or supporting documents current. The Hearing Panel shall prepare a proposed written decision, and if the Hearing Panel determines that a sanction should be imposed, the proposed written decision shall state the grounds for the sanction, and in the case of a suspension, the conditions for termination the suspension. A Party sanctioned under this Rule will have the right to appeal such a decision to the National Adjudicatory Council and ultimately to the NASD Board, in accordance with the Rule 9300 Series. If not timely appealed or called for review, the majority decision shall constitute final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1).

(b) Failure to Meet the Eligibility and Qualification Standards

The Hearing Officer may cancel the membership of any member who is ineligible for continuance in membership because it does not meet the eligibility and qualification standards set forth in Article III of the By-Laws. The Hearing Officer shall prepare a proposed written decision, and if the Hearing Officer determines that a cancellation should be imposed, the proposed written decision shall state the grounds for the cancellation. A member canceled under this Rule will have the right to appeal such a decision to the National Adjudicatory Council and ultimately to the NASD Board, in accordance with the Rule 9300 Series. If not timely appealed or called for review, the majority decision shall constitute final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1).

9544. Defaults

Respondents may file motions for reinstatement with the head of the department that issued the original pre-suspension notice under Rules 9541(a) or (b) within six months of the date of the original pre-suspension notice. If such a notion is filed, a Hearing Panel will be convened under Rule 9542, and the Hearing Panel may impose any fitting sanction. Respondents who are suspended pursuant to Rules 9541(a) or (b) and who fail to request hearing to challenge the suspensions within six months or receipt of the pre-suspension notice issued Rules 9541(a) or (b) will automatically be barred or expelled.

9545. Notice to Membership

The Association shall provide notice of a suspension, expulsion, cancellation, or bar under this Rule Series and the grounds therefor in the next membership supplement.

9546. Copies of Notices and Decisions to Member

A copy of a notice or decision under the Rule 9540 Series that is served on a person associated with a member shall be served on such member.

9547. Other Action Not Foreclosed

Action by the Association under the Rule 9540 Series shall not foreclose action by the Association under any other Rule.

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Disciplinary Actions

Disciplinary Actions Reported For August

NASD Regulation, Inc. (NASD Regulation®) has taken disciplinary actions against the following firms and individuals for violations of National Association of Securities Dealers, Inc. (NASD®) rules; federal securities laws, rules, and regulations; and the rules of the Municipal Securities Rulemaking Board (MSRB). Unless otherwise indicated, suspensions will begin with the opening of business on Monday, August 16, 1999. The information relating to matters contained in this *Notice* is current as of the end of July 21, 1999.

Firm Expelled

Block Trading, Inc. (CRD #36666, Houston, Texas) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm was censured and expelled from NASD membership. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it engaged in securities business when its net capital was below the required minimum and, acting through certain of its representatives, distributed a private placement memorandum to investors that contained false and misleading financial information and provided false and misleading information to prospective investors of the firm. The findings also stated that the firm, acting through certain representatives, failed to prepare and maintain accurate books and records in that false and misleading entries were made to the firm's general ledger and false and inaccurate FOCUS Part II filings were made in connection with the entries to conceal the firm's negative net capital position. The findings also stated that the firm, acting through certain representatives responsible for accounting and financial reporting, failed and neglected to provide notification that its net capital was below the required minimum. **(NASD Case #C05990031)**

Firm And Individual Barred Or Suspended

La Jolla Capital Corporation n.k.a. Pacific Cortez Securities Incorporated (CRD #24341, San Diego, California) and **Harold Bailey Gallison (CRD #1040211, Registered Principal, Las Vegas, Nevada).** The firm and Gallison were censured, barred from engaging in penny stock transactions in any capacity, fined $297,380, jointly and severally, fined $50,000 each individually, and required to present proof of restitution or rescission to their damaged customers, jointly and severally. Gallison was also barred in all principal and supervisory capacities, and suspended in all capacities for 30 days. The sanctions were based on findings that the firm and Gallison violated the Securities and Exchange Commission's (SEC) penny stock rules by failing to make adequate disclosure to their customers who purchased penny stocks. In addition, the firm and Gallison failed to establish, maintain, and enforce written procedures reasonably designed to detect and prevent violations of the penny stock rules. **(NASD Case #C02960001)**

Firms Fined, Individuals Sanctioned

Patterson Travis, Inc. (CRD #16540, Woodmere, New York), David Thomas Travis (CRD #448950, Registered Principal, Englewood, Colorado), and **Judah Liev Wernick (CRD #1633006, Registered Principal, Woodmere, New York)** submitted an Offer of Settlement pursuant to which the firm, Travis, and Wernick were censured and fined $10,000, jointly and severally, and ordered to comply with undertakings which include, among other things,

submitting a written agreement to the NASD. The written agreement will clearly delineate all of the terms of an arrangement including, but not limited to, a detailed list of expenses, by category, which are the obligation of the firm and those which are the obligation of Wernick or some other entity of the firm. The agreement will also permit the NASD to review the financial documentation and information concerning the payment of expenses of the entity and/or the individual paying the firm's expenses for the New York office. The firm and Wernick were fined an additional $30,000, jointly and severally, and Wernick was fined an additional $20,000, suspended from association with any NASD member in any capacity for 10 business days, and suspended from association with any NASD member in any managerial or supervisory capacity for 60 days thereafter. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, directly and acting through Travis and Wernick, received payments for the purchase of securities from public customers prior to the effective date of an initial public offering. The findings also stated that the firm, directly and acting through Wernick, failed to execute promptly customer orders to purchase or sell shares of common stock and failed to promptly and/or accurately report its transactions in the stock. **(NASD Case #C8A980095)**

Sedgwick Investments, Inc. (CRD #35045, Memphis, Tennessee), Michael Joseph Reilly (CRD #2150716, Registered Principal, Spokane, Washington), Pattie Jane Robinson (CRD #2484162, Registered Representative, Memphis, Tennessee), and **William Ellett Allen (CRD #2916388, Associated Person, Memphis, Tennessee)** submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm and Reilly were censured and fined $12,500, jointly and severally, and Reilly was suspended from association with any NASD member in any capacity for two weeks. Robinson and Allen were each censured, fined $5,000, and suspended from association with any NASD member in any capacity for two weeks. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that while associated with the firm, Robinson was actively engaged in the management of the firm's securities business, prior to her becoming registered with the NASD in any principal capacity and engaged in the firm's securities business prior to becoming registered in any capacity with the NASD. The findings also stated that Allen was associated with the firm and was actively engaged in the management of the firm's securities business as a financial and operations principal prior to his becoming registered with the NASD in the appropriate capacity, and that the firm, acting through Reilly, its president, failed to ensure that all persons who were actively engaged in the firm's securities business, or in the management thereof, were properly registered with the NASD. In addition, the NASD determined that the firm failed to establish, maintain, and enforce supervisory procedures that would ensure the proper registration of persons actively engaged in the firm's securities business, or in the management thereof, and the firm, acting through Reilly, failed and neglected to complete a training needs analysis and to develop a written formal training plan concerning the Firm Element of the Continuing Education Program. **(NASD Case #C05990025)**

Firms And Individuals Fined

National Securities Corporation (CRD #7569, Seattle, Washington) and **Steven Alan Rothstein (CRD #818658, Registered Principal, Wilmette, Illinois)** submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm was censured and fined $51,000, and Rothstein was censured and fined $30,000. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm sold shares of an initial public offering that traded at a premium in the secondary market (a "hot issue") to investment partnerships and corporations and other like accounts without obtaining information on all persons having a beneficial interest in the accounts or obtaining assurances of counsel or accountant ensuring no restricted individuals had a beneficial interest in the accounts. In addition, the NASD found that the firm, acting through Rothstein, granted selling concessions, discounts, or other allowances to public customers involved in initial public offerings and permitted certain customers to obtain prices below the public offering price. The NASD also found that the firm reported transactions to the Automated Confirmation Transaction Service℠ (ACT℠) in violation of applicable securities laws and regulations regarding trade reporting, failed to accept transactions within 20 minutes of the trade being reported to ACT, and failed to establish, maintain, and enforce written procedures reasonably designed to achieve compliance with applicable securities laws and regulations. **(NASD Case #C3B990020)**

Orenstein Securities, Inc. (CRD #26511, Milwaukee, Wisconsin) and **William Henry Orenstein (CRD #2057208, Registered Principal, Milwaukee, Wisconsin)** submitted a Letter of Acceptance, Waiver, and Consent pursuant to which they were censured and fined $10,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that in connection with the sale of limited partnership interests, the firm, acting through Orenstein, failed to specify in the private placement memoranda a time by which all of the units had to be sold, failed to return investors' funds or take other appropriate action when all units were not sold by the stated date, withdrew funds from an account prior to the required number of units being sold in bona fide transactions, and failed to escrow funds properly. Moreover, the NASD found that the firm, acting through Orenstein, failed to disclose on a private placement memorandum the maximum number of units that Orenstein, one of the general partners, could purchase, failed to specify on another memorandum the maximum number of units Orenstein could purchase and the amount of supplemental financing he could secure in the event that all units were not sold. In addition, the firm, acting through Orenstein, filed inaccurate FOCUS IIA reports with the NASD in that, among other things, the reports overstated the firm's excess net capital. **(NASD Case #C8A990048)**

Thomas F. White & Co., Incorporated (CRD #7661, San Francisco, California), Robert Thomson Angle (CRD #811495, Registered Principal, San Francisco, California), and **Peter William Shea (CRD #420778, Registered Principal, Alameda, California)** submitted an Offer of Settlement pursuant to which they were censured and fined $20,000, jointly and severally, and the firm and Angle were separately fined $30,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Angle and Shea, failed to establish and implement adequate written supervisory procedures in order to detect and prevent unsuitable transactions with respect to the accounts of public customers and to supervise an individual's activities in connection with those accounts. The findings also stated that the firm, acting through Angle, entered into settlement agreements with customers that contained confidentiality clauses which prohibited or discouraged those customers from discussing the settlements with or disclosing the underlying facts to the NASD and other regulators. **(NASD Case #C01980016)**

Firms Fined

Berthel Fisher & Company Financial Services, Inc. (CRD #13609, Cedar Rapids, Iowa) submitted a Letter of Acceptance, Waiver, and Consent pursuant to 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 report written customer complaints received as required by the NASD, and failed to report specific disclosure events within 10 business days to the NASD. The findings also stated that the firm failed to file amended Forms U-4 and U-5 for the individuals subject to the complaints within 30 days of becoming aware of the facts or circumstances giving rise to a need for the amendments. **(NASD Case #C04990026)**

Donaldson, Lufkin & Jenrette Securities Corp. (CRD #7554, New York, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm was censured and fined $11,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it reported transactions to the Fixed Income Pricing System℠ (FIPS®) in violation of applicable securities laws and regulations regarding transaction reporting. The findings also stated that the firm failed to establish, maintain, and enforce written supervisory procedures reasonably designed to achieve compliance with applicable securities laws, regulations, and NASD rules relating to transaction reporting of high yield corporate bonds to the NASD. **(NASD Case #CMS990063)**

Johnson Rice & Company L.L.C. (CRD #19524, New Orleans, Louisiana) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm was censured, fined $7,500 jointly and severally with an individual, and fined an additional $18,500. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to require all covered employees to complete the Firm Element of the Continuing Education requirement; failed to conduct an annual compliance meeting; and failed to establish, maintain, and enforce proper supervisory procedures governing contingency offerings, ACT trade reporting, locked and crossed market procedures, and harassment of traders. The findings also stated that the firm failed to indicate on limit order tickets the order terms and conditions to reflect that they were "not held" orders, failed to designate trades as short sales by including the appropriate .S modifier, and failed to denote on the firm's books and records an affirmative determination that the

subject securities could be borrowed. Furthermore, the NASD determined that the firm reported transactions to ACT in violation of applicable securities laws and regulations regarding trade reporting, failed to designate securities trades as late, and failed to report Nasdaq National Market® securities transactions accurately. The NASD also determined that the firm, in connection with a contingency offering, failed to establish a proper bank escrow account and continued to sell partnership interests after the offering termination date. **(NASD Case #C05990022)**

McDonald & Company Securities, Inc. n.k.a. McDonald Investments Inc. (CRD #566, Cleveland, Ohio) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm was censured, fined $7,500, and required to provide restitution, plus interest, of $7,931.40 to public customers. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it sold shares of securities to public customers and, at the time that the transactions were executed, failed to use reasonable diligence to ascertain the best inter-dealer market for the securities so that the resultant prices to the customers were as favorable as possible under prevailing market conditions. **(NASD Case #CMS990064)**

Security Dealers Guild, Inc. (CRD #28437, Tarrytown, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to 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 order tickets that either contained inaccurate time stamps or no time stamps whatsoever, failed to include the appropriate notation as to the underlying accounts into which the trade was to be divided on order tickets, and failed to include a notation as to whether the trade, from the customer's viewpoint, was being done "long" vs. "short." The findings also stated that the firm failed to include an affirmative determination as to the firm's ability to borrow the underlying security on order tickets for short sales, failed to include the trade price reported to Nasdaq in customer confirmations for trades done on a risk basis, and the difference, if any, between the trade reported price to Nasdaq and the net price to the customer in the transaction. Furthermore, the NASD determined that the firm failed to include the amount of markup, markdown, or similar remuneration on confirmations for trades done on a riskless basis, or disclosed an inaccurate amount of markup/markdown to the customer, and had no written supervisory procedures in place to address the topics of trade reporting, marking of customer sell order tickets "long" vs. "short," and making appropriate affirmative determination and denoting same on order tickets. **(NASD Case #C10990103)**

Tucker Anthony Incorporated (CRD #837, New York, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which the firm was censured, fined $16,000, and ordered to pay restitution and interest of $497.09 to public customers. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it reported transactions to ACT and SelectNet℠ in violation of applicable securities laws and regulations regarding trade reporting, customer orders, and limit orders. The firm failed to use reasonable diligence to ascertain the best inter-dealer markets for securities so that the resultant prices to the customers were as favorable as possible under prevailing market conditions and failed to display immediately customer limit orders when the orders were at a price that would have improved the firm's bid or offer in each security related to the orders. The findings also stated that the firm failed to establish, maintain, and enforce written supervisory procedures reasonably designed to achieve compliance with applicable securities laws, regulations, and NASD rules relating to trade reporting, ACT rules, locked and crossed markets, the use of the Small Order Execution System℠(SOES℠), anti-competitive practices, the Limit Order Protection Interpretation, and the SEC's Order Handling Rules. **(NASD Case #CMS990055)**

Individuals Barred Or Suspended

Solomon Jack Algazi (CRD #2162632, Registered Representative, Brooklyn, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $15,000, and suspended from association with any NASD member in any capacity for 18 months. Without admitting or denying the allegations, Algazi consented to the described sanctions and to the entry of findings that, during the course of an on-the-record interview, he failed to respond in a timely and complete manner with respect to questions asked of him by the NASD concerning his employment with a member firm. **(NASD Case #C10990104)**

Nicholas Mario Antonelli (CRD #2459572, Registered Representative, Hauppague, New York) and **Alexander Velez (CRD #2366712, Registered Representative, Brentwood, New York)** submitted an Offer of Settlement pursuant to which Antonelli was censured, fined $7,000, suspended from association with any NASD member

in any capacity for 45 days, and required to pay $2,000, plus interest, in restitution to a public customer; Velez was censured, fined $5,000, suspended from association with any NASD member in any capacity for 30 days, and required to pay restitution in the amount of $2,000, plus interest, to the customer. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that Antonelli and Velez failed to obey public customers' instructions to sell securities. The findings also stated that Antonelli engaged in unauthorized transactions, failed to obey his customer's instructions to sell securities, and prepared inaccurate books and records. In addition, Velez prepared inaccurate Forms U-4. **(NASD Case #C10980093)**

Ivan Douglas Bauer (CRD #1715502, Registered Representative, Penryn, California) submitted an Offer of Settlement pursuant to which he was censured, fined $52,900, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Bauer consented to the described sanctions and to the entry of findings that he participated in private securities transactions without providing prior written notification to, and obtaining approval from, his member firm. **(NASD Case #C01980021)**

Patrick Albert Beadle (CRD #2707932, Registered Representative, Oakland, California) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Beadle failed to respond to NASD requests for information. **(NASD Case #C01980019)**

Nicholas Bosco (CRD #2176953, Registered Principal, Colts Neck, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $12,500, suspended from association with any NASD member in any capacity for 60 days, barred from association with any NASD member in any principal capacity, and required to pay $40,687 in restitution, jointly and severally. Without admitting or denying the allegations, Bosco consented to the described sanctions and to the entry of findings that a member firm, acting through Bosco, effected transactions in common stock as principal at prices that were unfair and unreasonable taking into consideration all of the relevant factors. The findings also stated that the firm, acting through Bosco, violated terms of its restrictive agreement by engaging in "penny stock" transactions; conducting business in a manner that required it to maintain net capital of not less than $100,000; participating in "firm-commitment" underwritings; and effecting more principal trades than permitted in the agreement. **(NASD Case #C9A990033)**

Jeffrey Stuart Brewer (CRD #2790875, Registered Representative, Princeton, New Jersey) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Brewer failed to respond to NASD requests to testify and to produce documents. **(NASD Case #CAF980097)**

David Briggs (CRD #1275493, Registered Representative, Hollywood, Florida) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $10,000, suspended from association with any NASD member in any capacity for 18 months, and required to disgorge $7,659.14 in referral fees to public customers. Without admitting or denying the allegations, Briggs consented to the described sanctions and to the entry of findings that he engaged in private securities transactions. According to the findings, Briggs failed to provide written notice to his member firm that he was referring customers who sought to purchase shares of securities away from the firm and was being compensated for the referrals, nor did he obtain approval from his member firm for these activities. **(NASD Case #C07990040)**

Bartholomew Frank Bruno (CRD #2163217, Registered Principal, Forest Hills, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $12,500, suspended from association with any NASD member in any capacity for 60 days, barred from association with any NASD member in any principal capacity, and ordered to pay restitution of $40,687, jointly and severally, to public customers. Without admitting or denying the allegations, Bruno consented to the described sanctions and to the entry of findings that a member firm, acting through Bruno, effected transactions in common stock as principal at prices that were unfair and unreasonable taking into consideration all of the relevant factors. The findings also stated that the firm, acting through Bruno, violated terms of its restrictive agreement by engaging in "penny stock" transactions; conducting business in a manner that required it to maintain net capital of not less than $100,000; participating in "firm-commitment" underwritings; and effecting more principal trades than permitted in the agreement. **(NASD Case #C9A990031)**

Luis Bulas, Jr. (CRD #1684464, Registered Principal, Coral Gables, Florida) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were

based on findings that Bulas failed to respond to NASD requests for information. **(NASD Case #C07990005)**

Timothy Robert Calkins, Jr. (CRD #2469112, Registered Representative, Tobyhanna, Pennsylvania) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Calkins failed to respond to NASD requests for information. **(NASD Case #C9A990011)**

Carmen Robert Chimera (CRD #2585370, Registered Representative, Rockville, Maryland) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $5,000, suspended from association with any NASD member in any capacity for 14 days, which shall be deemed to have been served by virtue of the 14-day suspension imposed against him by his member firm. Without admitting or denying the allegations, Chimera consented to the described sanctions and to the entry of findings that he allowed another registered representative to sign variable annuity applications as the registered representative of record, falsely indicating that the representative had sold the variable annuities, when, in fact, they had been sold by Chimera. **(NASD Case #C9B990010)**

Paul Joseph Cilmi (CRD #2138510, Registered Principal, Brooklyn, New York) was censured, fined $50,000, barred from association with any NASD member in any capacity and ordered to disgorge earnings in the amount of $207,006.84. The sanctions were based on findings that Cilmi had an impostor take the Series 24 qualifications exam on his behalf. Cilmi also failed to appear for an on-the-record interview. **(NASD Case #C10980123)**

Jeff Lynn Clark (CRD #2195163, Registered Representative, Wyandotte, Michigan) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $52,900, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Clark consented to the described sanctions and to the entry of findings that he received monies totaling $6,580 from public customers for the purpose of paying insurance premiums, and checks totaling $2,000 from a public customer that were to be deposited in her fixed annuity account. The NASD determined that Clark failed to follow the customers' instructions, and without the customers' knowledge or authorization, used the funds for his own benefit or for some purpose other for than the benefit of the customers. **(NASD Case #C8A990051)**

Cara Wagner Clarke (CRD #2871723, Registered Representative, Maysville, Kentucky) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which she was censured, fined $13,250, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Clarke consented to the described sanctions and to the entry of findings that she received $750 from a public customer for the purpose of depositing $100 in the customer's Roth Individual Retirement Account and $650 in the customer's cash account. The NASD found that Clarke failed and neglected to deposit the $650 in the cash account and, instead, deposited the amount in an account that she controlled, thereby converting the $650 to her own use and benefit, without the customer's knowledge or consent. **(NASD Case #C05990020)**

Thomas John Dalton (CRD #1182680, Registered Principal, Levittown, New York) submitted an Offer of Settlement pursuant to which he was censured, fined $40,000, suspended from association with any NASD member in any capacity for three months, required to requalify by exam for the Series 7, 24, and 63 registrations before again acting in those capacities, and required to qualify by exam for the Series 55 registration before acting in that capacity. In addition, Dalton must cooperate with the NASD in connection with its prosecution of a formal action to include meeting with the staff and preparing for testimony, and appearing and testifying truthfully in that action. Without admitting or denying the allegations, Dalton consented to the described sanctions and to the entry of findings that, acting on behalf of his member firm, he charged public customers markups and markdowns greater than five percent above his firm's contemporaneous cost, totaling approximately $457,764.59. The findings also stated that Dalton, acting on behalf of his firm, charged public customers markups or markdowns greater than 10 percent above his firm's contemporaneous cost, totaling approximately $282,740.64. Furthermore, the NASD found that, in connection with transactions, Dalton failed to disclose to the customers that the prices at which the firm was engaging in these transactions with its customers were not reasonably related to the prevailing market price of these securities; effected transactions that were unfair and unreasonable taking into consideration all of the relevant factors; induced the purchase or sale of securities by means of manipulative, deceptive, or other fraudulent devices or contrivances; made untrue statements of material fact, omitted to state necessary material facts; and engaged in acts, practices, or a course of business which operated as a fraud or deceit upon persons. **(NASD Case #CAF990002)**

Bradly J. Denham (CRD #2727078, Registered Representative, Billings, Montana) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $25,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Denham consented to the described sanctions and to the entry of findings that he failed to respond to NASD requests for information concerning a customer complaint. **(NASD Case #C3B990023)**

John Steven DeSane (CRD #2653943, Registered Principal, Mt. Sinai, New York) was censured, fined $175,880, barred from association with any NASD member in any capacity, and ordered to pay restitution to public customers in the total amount of $57,748.25, plus interest. The sanctions were based on findings that DeSane made material misrepresentations and omissions in order to induce public customers to purchase securities and made fraudulent price predictions in connection with his recommendations to, and solicitation of, customers to purchase securities. In addition, DeSane effected transactions in the account of a public customer without the prior authorization of the customer and failed to follow customer instructions to execute a sell order. **(NASD Case #C3A980071)**

Thomas Anthony DiEdwardo, Sr. (CRD #2524146, Registered Representative, Kenilworth, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $28,000, barred from association with any NASD member in any capacity, and ordered to disgorge $6,000 to the NASD. Without admitting or denying the allegations, DiEdwardo consented to the described sanctions and to the entry of findings that, while associated with a member firm, he placed telephone calls to a public customer during which he used obscene language. The findings also stated that DiEdwardo arranged to have an impostor take the Series 7 qualification exam on his behalf. **(NASD Case #C10990090)**

John Philip DiGiacomo (CRD #2023333, Registered Representative, New York, New York) submitted an Offer of Settlement pursuant to which he was censured, fined $15,000, barred from association with any NASD member in any principal or supervisory capacity, barred from association with any NASD member in any capacity with the right to reapply for association with any NASD member in any capacity (other than any principal or supervisory capacity) after a period of two years, and ordered to make restitution to his former member firm in the initial principal amount of $44,258, plus interest. Without admitting or denying the allegations, DiGiacomo consented to the described sanctions and to the entry of findings that, as proprietary trader for his member firm and in an effort to conceal substantial net short positions in his trading account, DiGiacomo created and submitted fictitious buy order tickets purporting to cover approximately the net short positions. **(NASD Case #C10980046)**

Anthony Frederick DiMaria (CRD #2286669, Registered Principal, Shirley, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $5,000, and suspended from association with any NASD member in any capacity for 10 days. Without admitting or denying the allegations, DiMaria consented to the described sanctions and to the entry of findings that a member firm, acting through DiMaria, violated the terms of its restrictive agreement by engaging in “penny stock” transactions; conducting business in a manner that required it to maintain net capital of not less that $100,000; participating in “firm-commitment” underwritings; and effecting more principal trades than permitted in the agreement. **(NASD Case #C9A990028)**

Timothy James Ennis (CRD #837093, Registered Representative, New Hope, Pennsylvania) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $10,000, and suspended from association with any NASD member in any capacity for 10 days. Without admitting or denying the allegations, Ennis consented to the described sanctions and to the entry of findings that he recommended and engaged in purchase and sale transactions in the account of a public customer and did not have reasonable grounds for believing that these recommendations and resultant transactions were suitable for the customer on the basis of her financial situation, investment objectives, and needs. The findings also stated that Ennis exercised discretion in the customer’s account without having obtained prior written authorization from the customer and prior written acceptance of the account as discretionary by his member firm. **(NASD Case #C9A990034)**

Gary Anthony Familathe, Jr. (CRD #2665609, Registered Representative, San Francisco, California) was fined $25,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Familathe failed to respond to NASD requests for information. **(NASD Case #C01990003)**

Robert Fitzpatrick (CRD #842159, Registered Principal, Trumbull, Connecticut) was censured, fined $2,500, and suspended from association with any NASD member in any capacity for five business days. The National Adjudicatory Council (NAC) imposed the sanctions following appeal of a New York District Business Conduct Committee (DBCC) decision and a cross-appeal by the NASD's Department of Enforcement. The sanctions were based on findings that Fitzpatrick failed to respond to NASD requests for information in a timely manner.

Fitzpatrick has appealed this action to the SEC and the sanctions are not in effect pending consideration of the appeal. **(NASD Case #C10970176)**

Mark Angelo Gassoso (CRD #2590007, Registered Principal, Old Bridge, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $5,000, and suspended from association with any NASD member in any capacity for 10 days. Without admitting or denying the allegations, Gassoso consented to the described sanctions and to the entry of findings that a member firm, acting through Gassoso, violated the terms of its restrictive agreement by engaging in "penny stock" transactions; conducting business in a manner that required it to maintain net capital of not less than $100,000; participating in "firm-commitment" underwritings; and effecting more principal trades than permitted in the agreement. **(NASD Case #C9A990032)**

Jeffrey Feridun Gencay (CRD #1601133, Registered Representative, Knoxville, Tennessee) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $136,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Gencay consented to the described sanctions and to the entry of findings that he received $25,200 in checks from public customers for the purpose of investing in securities, failed and neglected to execute, or promptly execute, the purchase of securities, and instead, deposited the checks into an account that he controlled, and retained the funds until a later date, thereby misappropriating $25,200, without the knowledge or consent of the customers. **(NASD Case #C05990028)**

Andrew Harold Geyer (CRD #1908957, Registered Representative, Kings Park, New York) submitted an Offer of Settlement pursuant to which he was censured, fined $30,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Geyer consented to the described sanctions and to the entry of findings that he effected, or caused to be effected, securities transactions in the account of a public customer without the knowledge or consent of the customer. Geyer also failed to respond to NASD requests for information. **(NASD Case #C10990050)**

Kenneth Dean Gilkison (CRD #1243962, Registered Representative, Simi Valley, California) was censured, fined $35,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Gilkison misappropriated funds totaling over $5,000 from his member firm's budget accounting and reporting system accounts for his personal use by making numerous automated teller machine cash withdrawals to pay personal expenses and, without authorization, paid himself fees for "office management." Gilkison also cashed a check that he received from an attorney who sublet part of his firm's office space, which should have been deposited in the firm's account, and used at least a portion of the funds to pay personal expenses. **(NASD Case #C02980074)**

Dedric Hillery Gill, III (CRD #1935821, Registered Representative, Cedar Creek, Nebraska) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $5,000, suspended from association with any NASD member in any capacity for 20 days, and ordered to pay restitution of $36,150. Without admitting or denying the allegations, Gill consented to the described sanctions and to the entry of findings that he engaged in private securities transactions without providing all forms of notice required by the NASD. **(NASD Case #C04990028)**

David Clark Gossling (CRD #2545451, Registered Representative, Mesa, Arizona) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $23,600, and suspended from association with any NASD member in any capacity for 30 business days. Without admitting or denying the allegations, Gossling consented to the described sanctions and to the entry of findings that he engaged in an outside business activity for compensation without providing his member firm with prompt written notice. **(NASD Case #C3A990034)**

Ross Scott Greenberg (CRD #1892294, Registered Representative, Kings Park, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $20,000,

suspended from association with any NASD member in any capacity for six months, and required to requalify by taking the Series 7 exam prior to acting again in that capacity. Without admitting or denying the allegations, Greenberg consented to the described sanctions and to the entry of findings that he purchased shares of securities in a public customer's account without the customer's prior knowledge or consent. The findings also stated that Greenberg made material misrepresentations to the customer regarding the use of margin, how it works, the high level of risk involved using this strategy, and lulled the customer into accepting and/or ratifying the unauthorized purchase of shares of a security. **(NASD Case #C10990114)**

Hanna Grzedzicakawalek (CRD #2610590, Registered Representative, Glen Cove, New York) submitted an Offer of Settlement pursuant to which she was fined $50,000, barred from association with any NASD member in any capacity, and ordered to pay $1,784 in restitution. Without admitting or denying the allegations, Grzedzicakawalek consented to the described sanctions and to the entry of findings that she received a $1,479 cash payment from a public customer to pay the annual premium for a life insurance policy, never transmitted this payment to the insurance company, and, instead, deposited the money in her personal bank account and began making monthly premium payments of $135 on the customer's policy. The findings also stated that Grzedzicakawalek made a total of $810 of such payments and converted the remaining $669 to her own use and benefit without the customer's knowledge or consent. In addition, Grzedzicakawalek received insurance checks totaling $1,115.39 payable to public customers representing premium refunds from canceled life insurance policies. Rather than transmitting these payments to the customers, the NASD determined that Grzedzicakawalek endorsed the checks, deposited them in her personal bank account, and then converted the resulting funds to her own use and benefit, without the customers' consent or authority. Grzedzicakawalek also failed to respond to NASD requests for information. **(NASD Case #C9B990002)**

Gregory Eliot Hall (CRD #2450067, Registered Principal, Brooklyn, New York) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Hall failed to respond to NASD requests to appear for an on-the-record interview and to produce documents. **(NASD Case #C10980094)**

Matthew Christopher Hawley (CRD #2560308, Registered Principal, Sleepy Hollow, New York) submitted an Offer of Settlement pursuant to which he was censured, fined $80,000, suspended from association with any NASD member in any capacity for 18 months, and ordered to pay $316,001.00 in restitution to public customers. Without admitting or denying the allegations, Hawley consented to the described sanctions and to the entry of findings that he made material misrepresentations and failed to disclose material facts to public customers in order to solicit them to purchase securities. The findings also stated that Hawley made fraudulent price predictions to public customers in connection with his recommendations and solicitations to purchase securities, and effected transactions in the accounts of public customers without the prior authorization of the customers. Hawley also failed to execute a sell order as instructed by a public customer. **(NASD Case #C3A990001)**

Suzanne Hobbie (CRD #1268699, Registered Principal, Tampa, Florida) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which she was censured, fined $10,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Hobbie consented to the allegations and the entry of findings that she failed to submit accurate Forms U-4 that disclosed unsatisfied judgments ordered against her. (**NASD Case #C07990042)**

Ronald Ray Hutchinson (CRD #1206688, Registered Representative, Lawton, Oklahoma) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $5,000, and suspended from association with any NASD member in any capacity for one year. Without admitting or denying the allegations, Hutchinson consented to the described sanctions and to the entry of findings that he received a check in the amount of $358.32 from a public customer as a premium payment on her insurance policies, misused the customer funds by failing and neglecting to timely remit the payment to his member firm, and instead, deposited the customer's check into his personal bank account, without the customer's knowledge or consent, and then submitted premium payments totaling $353.01. **(NASD Case #C05990027)**

Jeffrey Rowe Jones (CRD #2069103, Registered Representative, Baldwinsville, New York) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Jones failed to respond to

NASD requests for information. **(NASD Case #C11980015)**

Gene Alex Jung (CRD #2807594, Registered Representative, San Francisco, California) was fined $40,000 and barred from association with any NASD member in any capacity. The sanctions were based on findings that Jung submitted a Form U-4 in which he failed to disclose his criminal convictions. **(NASD Case #C01990001)**

Cari Diane King (CRD #2483508, Registered Representative, Dallas, Texas) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that King failed to respond to NASD requests for information and documentation regarding funds inadvertently deposited by her employer into her personal account which she refused to return. **(NASD Case #C06980026)**

Gerard William King (CRD #1840274, Registered Representative, Metuchen, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $75,000, barred from association with any NASD member in any capacity, and ordered to pay disgorgement of $148,511.41. Without admitting or denying the allegations, King consented to the described sanctions and to the entry of findings that he accepted bribes, in the form of shares of common stock, and, in return for the bribes, sold shares of the common stock to public investors. King also failed to appear for an on-the-record interview. **(NASD Case #C10990094)**

Jeffrey Scott Koch (CRD #2459924, Registered Representative, Rochester, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $88,750, barred from association with any NASD member in any capacity, and ordered to pay restitution to a public customer in the amount of $3,750, plus interest. Without admitting or denying the allegations, Koch consented to the described sanctions and to the entry of findings that he accepted an order to purchase shares of securities from a public customer, and received checks totaling $3,750 for payment of the securities. The NASD found that, instead of executing the purchase order as directed, Koch created a false confirmation of the purchase, mailed the false confirmation to the customer as evidence of an executed transaction when no such transaction had ever occurred, endorsed the checks, deposited them into his personal bank account, and used the funds for his own benefit. In addition, Koch failed to respond completely to NASD requests for information. **(NASD Case #C8B990018)**

Daniel Lawrence Kouba (CRD #1254972, Registered Representative, Hillsboro, Wisconsin) submitted an Offer of Settlement pursuant to which he was censured, fined $10,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Kouba consented to the described sanctions and to the entry of findings that he engaged in private securities transactions, and failed and neglected to provide prior written notice to, and obtain prior written authorization from, his member firm to engage in the transactions. **(NASD Case #C8A990018)**

Eric Thomas Landis (CRD #2605896, Registered Principal, Weston, Connecticut) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $35,000, and suspended from association with any NASD member in any capacity for one year. Without admitting or denying the allegations, Landis consented to the described sanctions and to the entry of findings that, acting in his capacity as a trader for a member firm, he engaged in manipulative, deceptive and/or fraudulent conduct by intentionally executing and reporting fictitious transactions to the Nasdaq National Market at or near the close of the market for the purpose of artificially affecting the reported last sale prices in the securities. The findings also stated that Landis intentionally published and circulated reports of purchase and sale transactions that he knew were fictitious and non-bona fide. **(NASD Case #CMS990061)**

Vincent Francis Laurino (CRD #2483765, Registered Representative, Old Bridge, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $7,500, and suspended from association with any NASD member in any capacity for two days. Without admitting or denying the allegations, Laurino consented to the sanctions and to the entry of findings that he sold a fixed annuity to public customers without the prior authorization or knowledge of his member firm. **(NASD Case #C10990093)**

Brian Chulyoung Lee (CRD #2677650, Registered Representative, Chino Hills, California) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Lee failed to respond to NASD requests for information. **(NASD Case #C02980080)**

George Cornelius LeFlore (CRD #1173833, Registered

Representative, Dixmore, Illinois) was censured, fined $55,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that LeFlore received a check in the amount of $5,209.95 from insurance customers with instructions to use such funds to correct problems with their insurance policies and to get a better return. LeFlore failed to follow said instructions and used the funds for some purpose other than for the benefit of the customers until he returned the funds at a later date. LeFlore also failed to respond to NASD requests for information. **(NASD Case #C8A980065)**

Michael Anthony Dupre Lucarelli (CRD #2253171, Registered Representative, Los Angeles, California) was censured, fined $15,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Lucarelli filed a false and misleading Form U-4 with the NASD that failed to disclose a customer complaint charging him and the firm with which he was then employed with fraudulently obtaining $225,000 to open a securities account and with conversion of that sum. **(NASD Case #C02980055)**

John Anthony Massaro (CRD #2629695, Registered Representative, Smithtown, New York) was censured and barred from association with any NASD member in any capacity. The sanctions were based on findings that Massaro made material misrepresentations, failed to disclose material facts, made fraudulent price predictions to public customers in connection with his solicitation to purchase securities, and effected transactions in the accounts of public customers without the prior authorization of the customers. The findings also stated that Massaro failed to execute sell orders as instructed by public customers and failed to respond to NASD requests for information. **(NASD Case #C3A980076)**

Machelle Rene May (CRD #2506083, Registered Representative, San Diego, California) was censured, fined $210,000, barred from association with any NASD member in any capacity, and ordered to pay restitution to her member firm in the amount of $5,000. The sanctions were based on findings that May made unauthorized electronic transfers totaling $42,208.67 from her firm's payroll account to her own bank account, failed to enter the transfers in her firm's records, and converted the funds to her personal use. **(NASD Case #C02990003)**

Edward Alloyisus McGilly, Jr. (CRD #2339846, Registered Principal, Saint James, New York) was censured, fined $125,000, barred from association with any NASD member in any capacity, and ordered to pay $113,721.25 in restitution to public customers. The sanctions were based on findings that McGilly made material misrepresentations and omitted to disclose material information in connection with the purchase and sale of securities. McGilly also provided public customers with price predictions without having a reasonable basis for making such projections, and effected transactions in the accounts of public customers without the customers' prior authorization and consent. **(NASD Case #C3A980042)**

James Anthony McInerney (CRD #2179456, Registered Representative, Centerport, New York) submitted an Offer of Settlement pursuant to which he was censured, fined $20,000, and barred from association with any NASD member in any capacity with the right to reapply in five years. Without admitting or denying the allegations, McInerney consented to the described sanctions and to the entry of findings that he either refused or failed to execute sell orders placed by public customers, and bought and/or sold securities for the accounts of customers without obtaining the customers' authorization. McInerney also required that customers purchase aftermarket shares as a condition of purchasing initial public offering units. **(NASD Case #CAF980031)**

Scott Evans McVicker (CRD #2275303, Registered Representative, Littleton, Colorado) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $7,500, and suspended from association with any NASD member in any capacity for one month. Without admitting or denying the allegations, McVicker consented to the described sanctions and to the entry of findings that he received funds from a public customer intended for the purchase of a variable annuity, failed to forward these funds to the member firm with which he was then registered, and instead, forwarded the annuity application and the funds to an individual associated with the broker/dealer with which he had made application to become registered. The findings also stated that McVicker participated in a private securities transaction without providing his member firm with prior written notice.

McVicker's suspension began July 19, 1999, and will conclude at the close of business on August 18, 1999. **(NASD Case #C3A990041)**

Socorro Maria Mendez (CRD #2858757, Registered Representative, Santa Ana, California) was censured, fined $25,000, and barred from

association with any NASD member in any capacity. The sanctions were based on findings that Mendez failed to respond completely and timely to an NASD request for documents and to appear for testimony. **(NASD Case #C02980094)**

Robert Mogavero (CRD #2449762, Registered Representative, Hypoluxo, Florida) was censured, fined $50,000, barred from association with any NASD member in any capacity, and ordered to disgorge commissions in the amount of $35,765.45 to the NASD. The sanctions were based on findings that Mogavero arranged to have an impostor take the Series 7 and Series 63 exams on his behalf. Mogavero also failed to appear for an on-the-record interview. **(NASD Case #C10990016)**

Richard John Nicola (CRD #2376561, Registered Principal, Brooklyn, New York) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $16,500, suspended from association with any NASD member in any capacity for 60 days, barred from association with any NASD member in any principal capacity, and required to pay $40,687 in restitution, jointly and severally. Without admitting or denying the allegations, Nicola consented to the described sanctions and to the entry of findings that a member firm, acting through Nicola, effected transactions in common stock as principal at prices that were unfair and unreasonable taking into consideration all of the relevant factors. The findings also stated that the firm, acting through Nicola, violated terms of its restrictive agreement by engaging in "penny stock" transactions; conducting business in a manner that required it to maintain net capital of not less than $100,000; participating in "firm-commitment" underwritings; and effecting more principal trades than permitted in the agreement. In addition, the firm, acting through Nicola, violated SEC penny stock transaction and disclosure rules and failed to properly prepare order tickets and confirmations for stock transactions. **(NASD Case #C9A990030)**

Boris Rentzer (CRD #2591601, Registered Representative, Staten Island, New York) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Rentzer failed to respond to NASD requests to provide testimony. **(NASD Case #C10980057)**

Samuel Jeffrey Rhoades (CRD #2277634, Registered Principal, Bellaire, Texas) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $50,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Rhoades consented to the described sanctions and to the entry of findings he created fictitious monthly account statements relating to a public customer and then forwarded those fictitious monthly account statements to the customer. Rhoades also failed to respond to an NASD request to provide testimony. **(NASD Case #C06990009)**

Patrick Kelton Roberts (CRD #2906143, Registered Representative, Van Buren, Arkansas) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $25,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Roberts consented to the described sanctions and to the entry of findings that he failed to respond to NASD requests for information. **(NASD Case #C04990025)**

Adam Bruce Salberg (CRD #1746502, Registered Representative, Rockway, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $2,500, and suspended from association with any NASD member in any capacity for 60 days. Without admitting or denying the allegations, Salberg consented to the described sanctions and to the entry of findings that he forged a public customer's name on an account application by cutting and pasting the customer's signature from another document without the customer's knowledge or consent. **(NASD Case #C9B990012)**

Eric Eugene Scherrer (CRD #2652030, Associated Person, Denver, Colorado) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Scherrer filed a Form U-4 with the NASD that failed to disclose that he had been charged with criminal felonies. **(NASD Case #C3A990005)**

Joseph Salvatore Tarulli (CRD #2629825, Registered Representative, Staten Island, New York) was censured, fined $25,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Tarulli failed to respond to NASD requests for information. **(NASD Case #C10980102)**

Adam Alexander Townsend (CRD #2072351, Registered Representative, Hoboken, New Jersey) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was

censured, fined $25,000, and barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Townsend consented to the described sanctions and to the entry of findings that he executed trades in the amount of $38,263.75 in the accounts of public customers without the customers' prior knowledge or consent. The findings also stated that Townsend settled a customer complaint concerning an unauthorized transaction by sending a check in the amount of $1,406.25 to a public customer without his firm's knowledge or consent. **(NASD Case #C10990092)**

Anthony Edward Verello (CRD #2578981, Registered Representative, Brooklyn, New York) was censured, fined $55,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Verello provided false information on an employment application by failing to disclose that he had been arrested on a charge of felony burglary in the third degree and had pled guilty to a misdemeanor criminal trespass charge. Verello also failed to respond to NASD requests for information. **(NASD Case #C10980081)**

James Thomas Walsh (CRD #2493819, Registered Representative, Commack, New York) was censured, fined $150,000, barred from association with any NASD member in any capacity, and ordered to pay $50,875, plus interest, in restitution to public customers. The sanctions were based on findings that Walsh made material misrepresentations and failed to disclose material facts to public customers in order to induce them to purchase securities. In addition, Walsh made fraudulent price predictions to the customers in connection with his recommendations and effected a transaction in a public customer's account without the prior authorization of the customer. **(NASD Case #C3A980044)**

Victoria Jean Williams (CRD #713566, Registered Representative, Sunset Beach, California) was censured, fined $15,000, and barred from association with any NASD member in any capacity. The sanctions were based on findings that Williams solicited a securities investment of $1,000 from a public customer, provided the customer with an "Explanation of Investment" form as a receipt, and misled the customer into believing that this was an investment in a securities fund. Instead, Williams improperly caused the customer's funds to be deposited into the account of her landlord without the customer's knowledge or consent and repaid the customer at a later date. **(NASD Case #C02980053)**

Heath Robert Youell (CRD #474764, Registered Representative, Seattle, Washington) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $300,000, barred from association with any NASD member in any capacity, and ordered to pay $54,959 in restitution to a public customer. Without admitting or denying the allegations, Youell consented to the described sanctions and to the entry of findings that he deposited $54,959 of a public customer's funds into a bank account under his control. Rather than purchase mutual funds for the customer as instructed, the NASD found that Youell used the funds for his own benefit without the authorization of the customer. **(NASD Case #C3B990025)**

Individuals Fined

Robert Gary Amos (CRD #1024719, Registered Representative, Selah, Washington) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured and fined $15,000. Without admitting or denying the allegations, Amos consented to the described sanctions and to the entry of findings that he failed to provide prompt written notice to either of his member firms that he would be accepting compensation for the sale of viatical settlements, which was outside the scope of his relationship with his employers. **(NASD Case #C3B990024)**

James Burling Chase (CRD #368743, Registered Principal, Milwaukee, Wisconsin) submitted an Offer of Settlement pursuant to which he was censured and fined $20,000. Without admitting or denying the allegations, Chase consented to the described sanctions and to the entry of findings that a member firm, acting through Chase, effected securities transactions when the firm failed to maintain its minimum required net capital, prepared inaccurate trial balances and net capital computations, and filed inaccurate FOCUS Part IIA reports with the NASD. The findings also stated that the firm, acting through Chase, failed to comply with the terms of its restrictive agreement when the firm processed more proprietary transactions in its inventory than permitted and also received and held customer securities in violation of the agreement. Furthermore, the NASD determined that the firm, acting through Chase, failed to employ a properly qualified financial and operations principal. **(NASD Case #C8A990009)**

Leonard John Ialeggio (CRD #254515, Registered Representative, Danville,

California) was censured, fined $15,000, and ordered to requalify by exam as a general securities representative. The U.S. Court of Appeals for the Ninth Circuit denied Ialeggio's petition for review of a May 1998 SEC decision and affirmed the sanctions imposed. The sanctions were based on findings that Ialeggio submitted expense vouchers to his member firm's parent company and received payment for travel expenses totaling $8,502.50, to which he was not entitled. Ialeggio also induced the company to pay $35,000 for his country club dues, a payment to which he was not entitled. **(NASD Case #C01930044)**

Mark Desean Odom (CRD #2194790, Registered Representative, Redmond, Washington) submitted a Letter of Acceptance, Waiver, and Consent pursuant to which he was censured, fined $7,500, and required to pay restitution to public customers in the total amount of $5,685. Without admitting or denying the allegations, Odom consented to the described sanctions and to the entry of findings that he recommended purchases and sales in the joint account of public customers without having reasonable grounds for believing such transactions were suitable for the customers in light of the facts disclosed by them as to their other security holdings, and their financial situation, objectives, and needs, and in light of the nature of the equities recommended, and the concentration of specific equities in the account created by Odom's recommendations. **(NASD Case #C3B990018)**

Complaints Filed

The following complaints were issued by the NASD. Issuance of a disciplinary complaint represents the initiation of a formal proceeding by the 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.

ACAP Financial, Inc. (CRD #7731, Salt Lake City, Utah) and **Kirk Lynn Ferguson (CRD #1307741, Registered Principal, Centerville, Utah)** were named as respondents in an NASD complaint alleging that the firm, acting through Ferguson, reported transactions to ACT as agency transactions when the transactions should have been reported as principal transactions, and reported short sale transactions with the incorrect short sale modifier. The complaint also alleges that the firm, acting through Ferguson, effected a transaction at an unfair price that was based upon an excessive markdown, and engaged in market-making activity during the restricted period of a distribution. The complaint alleges that Ferguson functioned in a registered or active capacity while inactive due to the Regulatory Element of the Continuing Education requirement. The complaint also alleges that the firm, acting through Ferguson, failed to file any reports of customer complaints to the NASD, and failed to establish, maintain, and enforce written supervisory procedures reasonably designed to achieve compliance with applicable laws, rules, and regulations. **(NASD Case #C3A990044)**

Christopher Michael Block (CRD #2073057, Registered Principal, Houston, Texas), Jeffrey Schwartz Burke (CRD #2007369, Registered Principal, Houston, Texas), and **Jennifer Lynn Gonzalez (CRD #2461482, Registered Principal, Houston, Texas)** were named as respondents in an NASD complaint alleging that Block and Gonzalez failed and neglected to ensure the preparation and maintenance of accurate books and records for their member firm, and failed and neglected to ensure the accurate preparation of FOCUS Part II filings for their firm. The complaint also alleges that Block, Burke, and Gonzalez allowed their firm to engage in a securities business when each knew, or should have known, that the firm's net capital was below the required minimum, and that Block and Gonzalez failed and neglected to provide notification that their firm's net capital was below the required minimum. The complaint further alleges that Block and Gonzalez induced the purchase of stock by providing financial information which they knew, or should have known, was false and misleading to public customers. The complaint also alleges that Block and Burke failed and neglected to exercise reasonable and proper supervision of Gonzalez, their firm's designated financial and operations principal. **(NASD Case #C05990026)**

Kenneth M. Caraglio (CRD #2580769, Registered Representative, Miami, Florida) was named as a respondent in an NASD complaint alleging that he purchased calls in the accounts of public customers and advised the customers that their calls had increased in value, after which the customers authorized Caraglio to sell their calls and purchase other calls he had recommended with the proceeds. The complaint alleges that Caraglio did not sell the original calls or purchase the options, and that the original calls expired worthless in each account. The complaint alleges that Caraglio then falsely represented to the customers that the calls he recommended had been purchased, provided the customers with a handwritten confirmation

falsely stating that the calls had been purchased, and falsely represented that their calls could be sold for a $23,000 profit. The complaint alleges that after the customers instructed him to sell the calls and to send a check for the proceeds, Caraglio falsely represented to the customers that the calls had been sold and provided each with a false copy of a sell ticket as evidence thereof, but neither customer ever received a check for the profit that Caraglio falsely represented they had made. The complaint also alleges that Caraglio failed to respond to NASD requests for information. **(NASD Case #C07990046)**

David Scott Eli (CRD #1717625, Registered Representative, Clarksburg, West Virginia) was named as a respondent in an NASD complaint alleging that he received checks from public customers totaling $53,259.16 for the purpose of making payments on life insurance policies or for the purpose of investing in interest-bearing instruments, negotiated the checks, but did not remit the proceeds for their intended purposes. The complaint also alleges that Eli failed to respond to NASD requests for information. **(NASD Case #C9A990035)**

Brett Adam Finkelstein (CRD #2387245, Registered Representative, Boca Raton, Florida) was named as a respondent in an NASD complaint alleging that he reimbursed a public customer for his unrealized loss in a stock without obtaining prior authorization from his member firm and without having ever contributed funds to the customer's account. Finkelstein's reimbursement constitutes an impermissible sharing in the losses in a customer's account. **(NASD Case #C10990100)**

Jeffrey Phillip Halling (CRD #2468671, Registered Representative, Eagan, Minnesota) was named as a respondent in an NASD complaint alleging that he received an annuity redemption check in the amount of $35,060 from a public customer, failed to follow the customer's instructions to purchase an index annuity, deposited the $35,060 check into his personal bank account, returned $15,500.42 to the customer, and without the knowledge or consent of the customer, converted the remaining $19,559.58 to his own personal use and benefit. The complaint also alleges that Halling received funds totaling $23,053 from other public customers with instructions to purchase various mutual funds, failed to purchase the mutual funds, and without the knowledge or consent of the customers, converted the $23,053 to his own personal use and benefit. The complaint also alleges that Halling failed to respond to NASD requests for information. **(NASD Case #C04990032)**

Frank Mark Paladino, Jr. (CRD #1503957, Registered Representative, Guilford, Connecticut) was named as a respondent in an NASD complaint alleging that he used a public customer's credit card without the customer's authorization, withdrew a total of $9,800 from the customer's account, and improperly converted the funds for his own use and benefit. **(NASD Case #C11990024)**

Michele Edwardia Posey (CRD #2435628, Registered Representative, Chicago, Illinois) was named as a respondent in an NASD complaint alleging that she withdrew $12,500 from the savings accounts of public customers, without the customers' knowledge or authorization, and used the funds for her own benefit or for some purpose other than for the benefit of the customers. The complaint also alleges that Posey failed to respond fully to NASD requests for information. **(NASD Case #C8A990059)**

Robert Tretiak (CRD #1416058, Registered Principal, Las Vegas, Nevada) was named as a respondent in an NASD complaint alleging that a member firm, acting through Tretiak, participated in an initial public offering of common stock on a contingency basis to raise funds to acquire a parcel of land, and provided a prospectus to public investors that was materially false and misleading in that it failed to disclose the fact that the land offering had already been purchased through a string of financial arrangements orchestrated by Tretiak. These events rendered false and misleading representations in the prospectus indicating that financing had not yet been obtained and, in fact, might not be needed if the maximum number of shares was sold. The complaint also alleges that the firm, acting through Tretiak, failed to return investor funds when terms of the contingency were not met and failed to transmit promptly investor funds to a properly established escrow account. **(NASD Case #C02990042)**

David Randall Wright (CRD #2378371, Registered Representative, Irving, Texas) was named as a respondent in an NASD complaint alleging that he placed orders to purchase shares of stock for his personal securities account with his member firm, failed to disclose to his firm that he was financially unable to pay for the shares, and failed to disclose that his intention was to pay for the shares by selling the shares prior to the settlement date and using the proceeds to cover the purchase price. The complaint also alleges that when questioned by his branch office manager about his financial ability to pay for his recent purchase, Wright represented that he could obtain the funds to pay for

this trade from his grandfather when, in fact, he had not discussed the stock purchase with his grandfather. The complaint also alleges that Wright caused the execution of transactions in his personal account for which he knowingly did not have the financial resources to settle, nor the ability to meet the initial margin requirements of Federal Reserve Board Regulation T, as well as the margin requirements set forth in the NASD's Conduct Rules. **(NASD Case #C06990008)**

Firms Expelled For Failing To Pay Fines, Costs, And/Or Provide Proof of Restitution In Connection With Violations

Aspen Capital Group, Inc., Denver, Colorado (June 30, 1999)

Lakeside Trading, Metairie, Louisiana (June 30, 1999)

Firms Suspended/Canceled

The following firms were suspended/canceled from membership in the NASD for failure to comply with formal written requests to submit financial information to the NASD. The actions were based on the provisions of NASD Rule 8210 and Article VII, Section 2 of the NASD By-Laws. The date the suspensions/cancellations 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.

Alexander Kale Securities, Inc., Geneva, Switzerland (July 7, 1999)

A.T.A.P. Financial Services, Inc., Leesburg, Florida (June 29, 1999 - July 9, 1999)

Individuals Whose Registrations Were Revoked For Failure To Pay Fines, Costs And/Or Provide Proof Of Restitution In Connection With Violations

Chan, Teresa Fei, Seattle, Washington (June 30, 1999)

Hawkins, Michael W., Atlanta, Georgia (June 30, 1999)

Jung, Jonathan K., Boston, Massachusetts (June 30, 1999)

Kauachi, William C., Houston, Texas (June 30, 1999)

Knight, Christopher S., Forest Hills, New York (June 30, 1999)

Loucks, Todd J., Oneonta, New York (July 16, 1999)

McNeil, Gerald C., North Bergen, New Jersey (June 30, 1999)

Montano, Daniel C., Orange, California (June 30, 1999)

Ong, Huang Huei, Singapore (June 30, 1999)

Russell, Thomas G., Metairie, Louisiana (June 30, 1999)

Salmonese, Benjamin V., New York, New York (June 30, 1999)

Spinelli, Jr., Frank John, Staten Island, New York (June 30, 1999)

NASD Regulation Hearing Panel Expels Monroe Parker Securities And Bars Principals; Fines In Excess Of $8 Million Imposed

NASD Regulation announced the expulsion of Monroe Parker Securities, Inc., Purchase, NY, from membership in the NASD and imposed a fine of $5.6 million for price manipulation, excessive markups, and other violations following a decision rendered by an NASD hearing panel.

Charged with fraud in connection with the sale of common stock, sanctioned, and fined are the following:

- **Alan S. Lipsky.** Monroe Parker's President was barred from associating, in any capacity, with any NASD member and fined: (i) $750,000 individually; (ii) $3.16 million jointly and severally with the firm, Bryan J. Herman, and Ralph J. Angeline for profits made trading Steven Madden, Ltd. Class A warrants; and (iii) $1.36 million jointly and severally with the firm and Herman for profits made trading United Leisure Corporation common stock.

- **Bryan J. Herman.** The firm's Vice President was barred from associating, in any capacity, with any NASD member and fined: (i) $1.1 million individually; (ii) $3.16 million jointly and severally with the firm, Lipsky, and Angeline for profits made trading Steven Madden, Ltd. Class A warrants; and (iii) $1.36 million jointly and severally with the firm and Lipsky for profits made trading United Leisure Corporation common stock.

- **Ralph J. Angeline**. The firm's Director of Trading was barred from associating, in any capacity, with any NASD member and fined: (i) $600,000 individually; and (ii) $3.16 million jointly and severally with the firm, Lipsky, and Herman for profits made trading Steven Madden, Ltd. Class A warrants.

Richard S. Levitov, the firm's Director of Compliance, was also charged with failure to supervise

and barred from associating with any member of the NASD in any principal capacity, suspended in all other capacities for one year, fined $5,000, and ordered to requalify by passing the Series 7 examination before re-associating with any member firm.

Collectively, taking into account that some of the fines have joint and several liability, the total amount imposed is $8,047,692, plus accrued interest. When fines are imposed with joint and several liability, both parties are responsible for the payment of the single dollar amount.

The complaint, filed on December 23, 1997, alleged that during late 1994 and early 1995, Monroe Parker, acting through Herman and Angeline, acquired approximately 94 percent of the Class A warrants of Steven Madden, Ltd. available for public trading. The significant majority of these warrants were acquired from Stratton Oakmont Securities, Inc.—Lipsky's and Herman's former employer and a firm expelled by NASD Regulation in December 1996. The hearing panel, comprised of a Hearing Officer and two industry members, found that after acquiring this dominant position, Monroe Parker manipulated the price of the warrants and, within six days, sold its entire inventory to its retail customers at fraudulently excessive markups.

More than $3 million in profits were made from these fraudulent trades—more than $2 million were made by the firm, while Lipsky and Herman personally profited by an additional $1.1 million. Once these profits were made, Monroe Parker no longer had an interest in artificially supporting the price, and reduced its bid for the security. Within a week, the price fell from $3.625 to $1.50 per warrant, and its customers lost millions of dollars.

The panel also found that Monroe Parker, Lipsky, and Herman fraudulently failed to disclose interests adverse to those of their customers in connection with the sale of a second security, United Leisure Corporation common stock. Customers who bought United Leisure stock, upon the firm's recommendation, were not told that the stock came from the personal accounts of Lipsky and Herman (who were previously given the stock at no cost by Monroe Parker, and who sold the stock back to the firm through pre-arranged trades). Lipsky and Herman personally profited from the sales by more than $1.3 million.

The panel additionally found that Lipsky and Levitov failed to supervise the trading and sales activity at Monroe Parker in violation of NASD Conduct Rules.

Angeline has appealed and the matter as to Levitov has been called for review by the NAC. The sanctions as to them are not in effect pending consideration by the NAC.

NASD Regulation Censures And Fines On-Site Trading, Inc. For Registration Violations

NASD Regulation announced that it censured and fined On-Site Trading, Inc., of Great Neck, NY, $25,000 for failure to properly qualify and register 14 individuals.

In addition to proprietary traders employed by the firm at its main trading floor in Great Neck, On-Site provides services to day-trading customers who effect trades from 10 On-Site branch offices and other remote locations around the country.

The censure and fine mark the first disciplinary action by NASD Regulation for violations of the NASD's Series 55 registration rule. The rule prohibits equity traders from trading in the Nasdaq® and over-the-counter markets without first passing a qualification examination for trading and market making and registering with NASD Regulation.

Without admitting or denying the charges, On-Site consented to the entry of findings that 14 employees who acted as equity traders between May 1, 1998, and January 31, 1999, failed to comply with the Series 55 registration rule. During that period, those 14 traders effected approximately 3,700 trades in 250 Nasdaq securities.

On-Site also consented to findings that it lacked adequate oversight to ensure proper registration of its traders. As part of the settlement, On-Site agreed to implement new compliance procedures to prevent future violations.

The Series 55 registration rule became effective in April 1998. It applies to Market Makers, agency traders, proprietary traders, and persons who supervise these activities. The rule was developed in response to concerns about rule violations by traders conducting market-making and principal trading functions in both the Nasdaq and over-the-counter markets.

In addition to the specialized Series 55 examination, equity traders must also have passed either the General Securities Registered Representative Examination (Series 7) or the Corporate Securities Limited Representative Examination (Series 62). The Series 55 examination includes questions regarding the Nasdaq market and Market Maker activities, automated execution and trading systems, trade reporting, and other industry regulations.

This matter resulted from an investigation conducted by NASD Regulation's New York District Office.

NASD Regulation Fines Pruco Securities $20 Million

Sales Practice, Advertising, Supervision, and Registration Violations Found in Connection with Variable Life Insurance Sales

NASD Regulation announced that it has censured and fined Pruco Securities Corporation, Inc., a broker/dealer subsidiary of The Prudential Insurance Company of America, $20 million for violations of federal securities laws and NASD rules which occurred in connection with the offer and sale of variable life insurance policies.

NASD Regulation found that sales of more than 200,000 Prudential variable life insurance policies from 1983 through 1995 violated NASD rules and federal securities laws. During this period, Pruco and its registered representatives:

- induced customers who already owned Prudential life insurance to purchase new variable life insurance policies by misrepresenting that the policies could be acquired for little or no additional cash payment, by using cash values and future dividends from customers' existing policies. In fact, those cash values and dividends often were insufficient to pay the premiums for new policies, and both the new and existing policies frequently lapsed when cash values and dividends were used to acquire new policies in this fashion;

- misrepresented, through misleading sales presentations, that premium payments would end, or "vanish," after a certain number of years;

- misrepresented that variable life insurance was not insurance but, instead, was an investment, savings, or retirement plan;

- made sales to customers for whom such sales were unsuitable, including persons who did not know they were purchasing insurance and persons who did not want to purchase insurance;

- used misleading and unauthorized sales literature to sell variable life insurance;

- failed to establish, maintain, and enforce reasonable supervisory procedures;

- failed to register representatives, enabling unregistered persons to sell securities, and failed to register principals; and

- failed to file or filed inaccurate Forms U-4 and U-5 which, among other things, provide disciplinary information to the investing public about registered representatives.

NASD Regulation found that these violations resulted from a breakdown of Pruco's procedures relating to the sale of life insurance products which are securities and that, despite repeated indications of problems, Pruco and Prudential Insurance Company failed to respond adequately.

"Securities firms that sell variable life insurance products must ensure that they are appropriate for particular investors and that brokers do not mislead their customers about the nature of these products. Both firms and representatives must realize that the same sales practice, supervisory and registration concerns that apply to traditional broker/dealer products also apply to variable life insurance," said NASD Regulation President, Mary L. Schapiro.

Variable life insurance is a hybrid product containing both insurance and securities elements. It guarantees a minimum death benefit but, unlike conventional life insurance, also provides a variable death benefit and a variable cash value reflecting the values of separate, segregated accounts of the insurance company. Through these accounts, which are invested in securities, the customer bears an investment risk. Because owners of variable life insurance policies assume investment risks, the policies are securities within the meaning of the federal securities laws. NASD Regulation has jurisdiction over the sale of variable life insurance by member firms and associated persons.

Customers who believed they were harmed by the sales practice violations covered by today's action, including those who purchased the more than 200,000 variable life insurance policies, have been able to participate in a remediation program instituted by Prudential Insurance Company in connection with settlements of actions by state insurance regulators and the settlement of a class action lawsuit. That program addressed sales of both fixed life insurance and variable life insurance. Prudential Insurance Company has taken an aggregate charge of $2.6 billion to provide the compensatory relief required by the remediation program. A significant portion of that relief relates to sales of variable life insurance.

In resolving this matter and imposing sanctions, NASD Regulation took into account the remediation program as well as actions taken by Pruco and Prudential Insurance Company to enhance and strengthen their policies and procedures.

As part of its settlement with NASD Regulation, Pruco, which neither admitted nor denied the allegations,

agreed to retain an outside consultant to review and make recommendations concerning the adequacy of the current policies and procedures of Pruco and Prudential Insurance Company. Pruco will implement necessary changes and submit a report to NASD Regulation detailing its actions.

This matter was investigated by NASD Regulation's Enforcement Department with assistance from its Advertising/Investment Companies Regulation Department. NASD Regulation wishes to acknowledge the cooperation and assistance of the State of Florida in this matter.

NASD Regulation Sanctions Trader For Limit Order Violations

NASD Regulation's National Adjudicatory Council (NAC) ordered Michael B. Jawitz to pay a $50,000 fine, be suspended from the securities industry for one year, and then requalify as an equities trader.

The NAC found that Jawitz engaged in deceptive conduct by entering fictitious limit orders into his member firm's order execution system that led to non-bona fide transactions. The NAC also found that by engaging in this type of conduct and violating the NASD's limit order protection rule, Jawitz abdicated his fiduciary responsibility by not protecting the customers' limit orders. The conduct occurred in 1995 and 1996.

Initially, NASD's Market Regulation Committee alleged that Jawitz engaged in manipulative, deceptive, or fraudulent conduct when he placed 184 fictitious limit orders in 30 Nasdaq stocks and then canceled them. While the Market Regulation Committee found that Jawitz placed fictitious limit orders, violated the NASD's limit order protection rule, and caused non-bona fide transactions to be publicly disseminated, the Market Regulation Committee, nevertheless, dismissed the charge that Jawitz did so with the intent to manipulate or defraud. Jawitz then appealed the other findings of the Market Regulation Committee to the NAC. When a case is appealed or called for review, the entire case – along with all the findings – is reviewed. In this instance, the NAC determined that Jawitz did indeed engage in deceptive conduct and reinstated the finding.

The NAC found that Jawitz engaged in deceptive conduct and intentionally prevented the execution of 75 customer limit orders in violation of the NASD's limit order protection rule. According to the limit order protection rule, brokerage firms must fill a customer's limit order before they trade the same securities for their own account at prices equal to or better than the customer limit order.

Jawitz entered fictitious limit orders into the firm's order execution system at superior prices in order to avoid having to execute customer limit orders that were already in the firm's system. The fictitious limit orders were executed and were reported to the Nasdaq quotation tape. Although Jawitz canceled the trades, dealers and public investors had no reason to believe that the reported transactions did not reflect legitimate trades and legitimate cancellations.

Jawitz has appealed this action to the SEC and the sanctions are not in effect pending consideration of the appeal.

NASD Regulation Fines Coleman & Company Securities, Inc. $200,000 For Unjustified Termination Of Firm Commitment Underwriting

NASD Regulation announced that an NASD Regulation Hearing Panel fined Coleman & Company Securities, Inc., New York, NY, $200,000 for violating NASD rules by backing out of a firm commitment underwriting of an initial public offering (IPO). The panel also suspended the firm for three months from participating in any underwritings, and for an additional nine months from acting as a lead managing underwriter.

On May 12, 1998, NASD Regulation filed a complaint against Coleman and its former president and CEO, Aaron Jones Yorke, IV. Yorke subsequently settled the matter, as described below. After Coleman's hearing, the panel found that it had acted as the managing underwriter for a November 20, 1995 IPO of 1 million shares of common stock of Hungarian Broadcasting Company (HBC) at $7 per share. According to the underwriting agreement, HBC was to receive net proceeds of $6.3 million from Coleman as a result of the offering. Despite Coleman's obligations to complete the offering and pay HBC, the hearing panel found that Coleman unjustifiably terminated the offering in violation of the NASD rule that requires member firms to observe high standards of commercial honor and just and equitable principles of trade in the course of doing business.

The hearing panel found that Coleman had terminated the offering because purchasers failed to affirm their orders when the price of HBC stock fell in the aftermarket,

and Coleman had insufficient capital to close the offering by purchasing the offered shares. Because of Coleman's termination, HBC did not receive any funds from the underwriting and all of the IPO purchases and aftermarket transactions had to be unwound and canceled, affecting at least 50 NASD member firms and their clearing agents. The hearing panel found that more than 230 customers had purchased HBC common stock in the initial public offering and that approximately 660,000 shares of HBC shares had traded in Nasdaq's SmallCap℠ market prior to the termination.

The hearing panel also ordered the firm to retain a consultant as a condition to resuming underwriting activity after the initial three-month suspension and to revise its compliance manual in accordance with the consultant's recommendations. HBC had previously filed a civil action against Coleman to recover the proceeds it was to receive under the underwriting agreement and subsequently settled that action.

NASD Regulation also previously entered into a settlement with Yorke, the former president and CEO of Coleman, for his role in the termination of the HBC offering. As part of that settlement, Yorke was fined $30,000, suspended from association with any member firm for 60 days, and censured. In submitting his Offer of Settlement, Yorke neither admitted nor denied the findings of NASD Regulation.

Coleman has appealed this action to the NAC and the sanctions are not in effect pending consideration of the appeal.

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For Your Information

Comment Period Extended

The Request for Comment period for *Notice to Members 99-54* has been extended until **August 31, 1999**, to give all interested parties, including those who may be focusing on issues relating to the deployment of Web CRD, a meaningful opportunity to comment.

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Join Us For The 1999 Fall Securities Conference.

At this event, you will learn about and discuss the latest developments in the securities industry. Also you will hear from industry experts and NASD Regulation leadership, explore regulatory issues, and much more.

Watch your mail for a conference brochure and registration materials. Questions? Call the NASD at (202) 728-8383 or visit the NASD Regulation Web Site.

www.nasdr.com

1999 NASD Regulation Fall Securities Conference

October 20 - October 22
Sheraton Seattle
Seattle, WA

Special NASD Notice to Members 99-74

Nominees For District 10 District Committee And District Nominating Committee

Suggested Routing

- ■ Senior Management
- ☐ Advertising
- ☐ Continuing Education
- ☐ Corporate Finance
- ■ Executive Representatives
- ☐ Government Securities
- ☐ Institutional
- ☐ Insurance
- ☐ Internal Audit
- ■ Legal & Compliance
- ☐ Municipal
- ☐ Mutual Fund
- ■ Operations
- ☐ Options
- ☐ Registered Representatives
- ■ Registration
- ☐ Research
- ☐ Syndicate
- ☐ Systems
- ☐ Trading
- ☐ Training
- ☐ Variable Contracts

National Association of Securities Dealers, Inc.
Notice Of Nominees

In accordance with the National Association of Securities Dealers, Inc. (NASD®) By-Laws, the purpose of this *Special Notice to Members* is to advise members of the nominees to fill vacancies on the District Committee and the District Nominating Committee in District 10 (New York). The individuals identified in this *Special Notice to Members* have been nominated for three-year terms on the District Committee and for one-year terms on the District Nominating Committee which begin in January 2000. (Nominees for Districts 1, 2, 3, 4, 5, 6, 7, 8, 9, and 11 were announced in *Special Notice to Members 99-62* that was mailed to members on July 15, 1999.)

We appreciate the interest shown by many of you in participating in the District Committees. We look forward to your participation in the matters of the Districts during the coming year. Following is a general description of the procedures pertaining to this stage of the election.

- If an officer, director, or employee of an NASD member is interested in being considered as an additional candidate, he/she must indicate his/her interest to the District Director within fourteen (14) calendar days of the date of this *Special Notice to Members*. The District Director shall make a written record of the time and date of such notification.

  If an additional candidate does not come forward after the 14 days, the election of the committee is complete.

  If an additional candidate does come forward within the 14 calendar days, the Secretary of NASD Regulation® will provide a list of all NASD members eligible to vote in the District and their Executive Representatives to the additional candidate immediately following receipt of the additional candidate's notice by the District Director.

- Additional candidate(s) may be nominated if a petition signed by the Executive Representative of at least 10 percent of the members eligible to vote in the District is filed with the District Nominating Committee within 30 calendar days from the mailing date of the list of members eligible to vote, unless the Secretary of NASD Regulation grants additional time for good cause shown. Only an Executive Representative may sign a petition on behalf of an NASD member.

- If no additional candidate(s) are nominated within the 30-calendar day period, then the candidates nominated by the District Nominating Committee shall be considered duly elected, and the District Committee shall certify the election to the Board of Directors of NASD Regulation.

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

Joan C. Conley
Corporate Secretary
National Association of Securities Dealers, Inc.
1735 K Street, N.W.
Washington, D.C. 20006-1500
(202) 728-8381

National Association of Securities Dealers, Inc.
District 10 District Committee Nominees And District Nominating Committee Nominees

The following persons have been nominated to serve on District 10 District Committee and District Nominating Committee.

District 10

David A. Leibowitz, District Director
NASD Financial Center
33 Whitehall Street
New York, NY 10004
(212) 858-4000

The five boroughs of New York City

District Committee Nominees

Kevin J. Browne
Banc of America Securities
New York, NY

Judith R. MacDonald
Rothschild Inc.
New York, NY

Stephen C. Strombelline
Barclays Capital Inc.
New York, NY

District Nominating Committee Nominees

Ralph J. Costanza
Salomon Smith Barney Inc.
New York, NY

Joan S. Green
BT Brokerage Corporation
New York, NY

Vicki Z. Holleman
Loeb Partners Corporation
New York, NY

Norman H. Pessin
Neuberger & Berman
New York, NY

Stuart J. Voisin
Stuart Coleman & Co. Inc.
New York, NY