

MARCH 2006

Notice to Members

Notices

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Disciplinary and Other NASD Actions



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Notice to Members

MARCH 2006

SUGGESTED ROUTING

Institutional
Legal & Compliance
Options
Senior Management
Trading
Training

KEY TOPICS

Exercise Limits
Options
Position Limits
Rule 2860

GUIDANCE

Options Position and Exercise Limits

Extension of Pilot Program Increasing Position and Exercise Limits for Stock Options

Executive Summary

On February 16, 2006, NASD filed for immediate effectiveness with the Securities and Exchange Commission (SEC) amendments to Rule 2860 extending until September 1, 2006, a pilot program increasing certain stock options position and exercise limits. The pilot program was scheduled to expire on March 3, 2006.

The rules, as amended, are set forth in Attachment A.

The amendments became effective February 16, 2006.

Questions/Further Information

Questions concerning this *Notice* may be directed to Gary L. Goldsholle, Vice President and Associate General Counsel, Office of General Counsel (OGC), Regulatory Policy and Oversight (RPO), at (202) 728-8104; or James L. Eastman, Assistant General Counsel, OGC, RPO, at (202) 728-6961.

Background and Discussion

On February 16, 2006, NASD filed for immediate effectiveness with the Securities and Exchange Commission (SEC) amendments to Rule 2860 extending until September 1, 2006, a pilot program increasing certain stock options position and exercise limits (Pilot Program).¹ The Pilot Program was scheduled to expire on March 3, 2006.² NASD extended the Pilot Program to allow it to continue without interruption.

06-09

NASD Rule 2860(b)(3)(A) imposes a ceiling or position limit on the number of conventional and standardized equity options contracts in each class on the same side of the market (i.e., aggregating long calls and short puts or long puts and short calls) that can be held or written by a member, a person associated with a member, a customer, or a group of customers acting in concert.³ The rule provides that the position limits for stock options are determined according to a five-tiered system in which more actively traded stocks with larger public floats are subject to higher position limits.

Pursuant to the Pilot Program, which began March 30, 2005, and now ends September 1, 2006, (unless extended) (Pilot Period), the limits for each of the tiers are as follows: (a) 13,500 contracts has been increased to 25,000 contracts, (b) 22,500 contracts has been increased to 50,000 contracts, (c) 31,500 contracts has been increased to 75,000 contracts, (d) 60,000 contracts has been increased to 200,000 contracts and (e) 75,000 contracts has been increased to 250,000 contracts. These tiers apply to both conventional and standardized options. Options exercise limits, which are set forth in Rule 2860(b)(4), and which incorporate by reference the position limits in Rule 2860(b)(3), also have been increased during the Pilot Period.

Endnotes

- 1 Securities Exchange Act Release No. 53346 (February 22, 2006), 71 FR 10580 (March 1, 2006) (SR-NASD-2006-025).
- 2 See Securities Exchange Act Release No. 52271 (August 16, 2005), 70 FR 49344 (August 23, 2005) (SR-NASD-2005-097) (extending Pilot Program); NASD Notice to Members 05-56 (August 2005). Securities Exchange Act Release No. 51520 (April 11, 2005), 70 FR 19977 (April 15, 2005) (SR-NASD-2005-040) (establishing Pilot Program); NASD *Notice to Members 05-31* (April 2005).
- 3 A "standardized equity option" is an equity options contract issued, or subject to issuance, by The Options Clearing Corporation that is not a FLEX Equity Option. NASD Rule 2860(b)(2)(VV). A "conventional option" is an option contract not issued, or subject to issuance, by The Options Clearing Corporation. NASD Rule 2860(b)(2)(N). NASD's limits on standardized equity options are applicable only to those members that are not also members of the exchange on which the option is traded; the limits on conventional options are applicable to all NASD members. NASD Rule 2860(b)(1)(A).

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ATTACHMENT A

New language is underlined.

2800. SPECIAL PRODUCTS

2860. Options

(a) No Change.

(b) Requirements.

(1) and (2) No Change.

(3) Position Limits

(A) Stock Options-Except in highly unusual circumstances, and with the prior written approval of NASD pursuant to the Rule 9600 Series for good cause shown in each instance, no member shall effect for any account in which such member has an interest, or for the account of any partner, officer, director or employee thereof, or for the account of any customer, non-member broker, or non-member dealer, an opening transaction through Nasdaq, the over-the-counter market or on any exchange in a stock option contract of any class of stock options if the member has reason to believe that as a result of such transaction the member or partner, officer, director or employee thereof, or customer, non-member broker, or non-member dealer, would, acting alone or in concert with others, directly or indirectly, hold or control or be obligated in respect of an aggregate equity options position in excess of:

(i) 13,500 (or 25,000 during the pilot period from March 30, 2005 through [March 3, 2006] September 1, 2006 ("Pilot Period")) option contracts of the put class and the call class on the same side of the market covering the same underlying security, combining for purposes of this position limit long positions in put options with short positions in call options, and short positions in put options with long positions in call options; or

(ii) through (viii) No Change.

(B) through (D) No Change.

(4) through (24) No Change.

Notice to Members

MARCH 2006

SUGGESTED ROUTING

Executive Representatives
Legal & Compliance
Operations
Senior Management
Systems

KEY TOPICS

NASD Sanction Guidelines

GUIDANCE

Sanction Guidelines

**NASD Revises Sanction Guidelines; Effective Date:
March 31, 2006**

Executive Summary

This *Notice* advises NASD members of modifications to the *NASD Sanction Guidelines* (Guidelines). NASD is amending the quality of markets guidelines and the guidelines for violations of Municipal Securities Rulemaking Board (MSRB) Rules G-36 and G-37. The new guidelines are effective as of March 31, 2006, and apply to all actions as of that date, including pending disciplinary cases.

The revised guidelines can be read in their entirety in Attachment A to this *Notice*. The revised guidelines are also available on NASD's Web site (www.nasd.com).

Questions/Further Information

Questions concerning this *Notice* may be directed to Carla Carloni, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8019.

Discussion

NASD initially published the Guidelines in 1993 to promote consistency and uniformity in the imposition of sanctions in disciplinary matters. Over the years, NASD has revised and updated the Guidelines and has adopted new individual guidelines in order to reflect changes in and additions to NASD's rules. NASD adjudicators rely on the Guidelines to determine appropriately remedial sanctions in disciplinary actions. NASD's Departments of Enforcement and Market Regulation and the defense bar also rely on the Guidelines in negotiating settlements in disciplinary matters. NASD therefore endeavors to maintain up-to-date and inclusive Guidelines that are designed to address a wide variety of potential violations of NASD's rules and provide fact-specific guidance for crafting appropriately remedial sanctions.

06-10

With these revisions, NASD seeks to increase the level of flexibility built into individual guidelines and to provide additional guidance as to mitigating and aggravating circumstances for individual violations. For example, NASD's trade reporting and other quality of markets guidelines previously grouped certain misconduct solely by whether it was a first, second or subsequent action. Under this prior structure, the recommended monetary sanction for *first* actions involving large numbers of violations or otherwise egregious misconduct tended to be at the low end of possible monetary sanctions. Similarly, the prior Guidelines categorized less egregious misconduct that happened to be a second or subsequent violation by recommending sanction ranges at the high end, regardless of whether other mitigating factors were present. In order to enhance flexibility, these revisions enable adjudicators and settling parties to take into account other important factors in addition to whether the respondent has a history of similar violations. The revisions refocus the analysis on important aggravating and mitigating factors in addition to disciplinary history and provide significant flexibility in sanction ranges.

NASD also is revising the monetary sanction ranges for many of the guidelines. NASD staff addresses less serious misconduct, misconduct that does not warrant a formal disciplinary proceeding, through letters of caution, compliance conferences and other informal means. Further, in certain situations, matters that warrant formal action may be handled through the Minor Rule Violation (MRV) plan. The Guidelines are intended to address misconduct that rises to the level of warranting formal action. The revisions conform the Guidelines to this concept by increasing the low end of recommended sanction ranges for first violations to \$5,000. An increase to \$5,000 of the low end of monetary sanction ranges will preserve the deterrent effect of NASD's sanctions and ensure that the guidelines are "significant enough to prevent and discourage future misconduct by a respondent, to deter others from engaging in similar misconduct, and to modify and improve business practices." –*NASD Sanction Guidelines*, General Principal No. 1. Similarly, the recommended fine range for a second action should send a clear message about the need for improvement after settling a first action. By recommending \$10,000 as the starting point of the fine range for a second action, the revised guidelines seek to deter repeat violations. Additionally, the revised guidelines indicate that, in cases involving egregious misconduct and multiple violations that harm the investing public, adjudicators (or settling parties) may consider imposing a fine on a per violation basis.

With these revisions, NASD aims to clarify for the membership the numerous considerations that directly affect the dollar amount of monetary sanctions imposed in disciplinary actions. NASD also seeks to provide additional guidance by modifying monetary sanction ranges and expanding monetary sanction options.¹

Effective Date

The amendments to the Guidelines are effective as of **March 31, 2006**, and apply to all actions as of that date, including pending disciplinary cases.

Endnotes

- 1 The revisions also include ministerial changes. For instance, NASD deleted from certain individual guidelines the statement that adjudicators may increase the recommended fine amount by adding the amount of a respondent's financial benefit. NASD did not delete this statement because it no longer applies to the determination of monetary sanctions for the violations at issue. Rather, NASD deleted the statement solely because it already is included in General Principle No. 6 in the introductory section of the Guidelines. Like all General Principles, General Principle No. 6 applies to the determination of monetary sanctions for all violations.

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ATTACHMENT A

Additions are underlined and deletions are in brackets.

Anti-Intimidation/Coordination—Failure to Comply with Rule Requirements

NASD Conduct Rule 2110 and IM-2110-5

<u>Principal Considerations in Determining Sanctions</u>	<u>Monetary Sanction</u>	<u>Suspension, Bar, or Other Sanctions</u>
<p><u>See <i>Principal Considerations In Introductory Section</i></u></p> <ol style="list-style-type: none"> 1. Whether the behavior was collusive or part of a larger manipulation. 2. Whether the behavior attempted to affect or actually affected publicly disseminated quotes or otherwise inhibited market transparency. 3. Whether the behavior attempted to or actually resulted in late or inaccurate trade reporting. 4. Whether the behavior attempted to or actually altered market prices. 5. In the case of intimidation or harassment, nature and content of respondent's speech, communications, and/or harassing behavior. 6. The general effect of the behavior on the fair and efficient operation of the securities markets. 7. Whether the behavior was repetitive or a single impulsive action. 	<p><u>Intimidation/ Harassment</u></p> <p>Fine of <u>\$5,000</u> [\$1,000] to \$50,000.</p> <p>In egregious cases, consider a fine in excess of \$50,000.</p> <p><u>Coordination</u></p> <p>Fine of \$10,000 to \$100,000.</p> <p>In egregious cases, consider a fine in excess of \$100,000.</p>	<p><u>Intimidation/Harassment</u></p> <p>In egregious cases, suspend individual respondent in any or all capacities and/or member firm respondent with respect to any or all activities or functions for a period of 10 business days to two years.</p> <p>In egregious cases involving intimidation, consider barring individual respondent.</p> <p><u>Coordination</u></p> <p>Suspend individual respondent in any or all capacities and/or member firm respondent with respect to any or all activities or functions for a period of 30 business days to two years.</p> <p>In egregious cases, consider expelling the member firm and/or barring individual respondent.</p>

Backing Away

NASD Conduct Rules 2110 and 3320, and IM-3320¹

Principal Considerations in Determining Sanctions	Monetary Sanction ²	Suspension, Bar, or Other Sanctions
<p><u>See <i>Principal Considerations in Introductory Section</i></u></p> <ol style="list-style-type: none"> Whether respondent offered contemporaneous trades or otherwise remediated the failures to execute. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p><i>First Action</i>^{3[2]} Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.⁴</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years.</p>

¹ This guideline also is appropriate for violations of MSRB Rule G-13.

² In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

³ [2] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.

⁴ If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Best Execution—Failure to Comply with Requirements for Best Execution

NASD Conduct Rules 2110 and 2320¹

Principal Considerations in Determining Sanctions	Monetary Sanction ²⁽¹⁾	Suspension, Bar, or Other Sanctions
<p><u>See <i>Principal Considerations in Introductory Section</i></u></p> <ol style="list-style-type: none"> Nature of the best execution violation, i.e., whether the execution was at an inferior price or was untimely. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p><u>Negligent Misconduct</u></p> <p><u>First Action</u>³ Fine of <u>\$5,000</u> [2,500] to <u>\$50,000</u>.</p> <p><u>Second Action</u> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u> [75,000].</p> <p><u>Subsequent Actions</u> Fine of <u>\$10,000</u> [7,500] to <u>\$200,000</u> [100,000] ^{4 [3]}</p> <p><u>Intentional Or Reckless Misconduct</u></p> <p>Fine of <u>\$20,000</u> [10,000] to <u>\$200,000</u> [100,000].</p> <p>In egregious cases, consider a fine <u>in excess of \$200,000</u>.</p>	<p><u>Negligent Misconduct</u></p> <p>In egregious cases, consider suspending the responsible individual in any or all capacities and/or the firm with respect to any or all activities or functions for up to 30 business days.</p> <p><u>Intentional or Reckless Misconduct</u></p> <p>Suspend responsible individual in any or all capacities and/or suspend firm with respect to any or all activities or functions for a period of 10 business days to two years.</p> <p>In egregious cases, consider barring the individual and/or expelling the firm.</p>

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- 1 This guideline may also be appropriate for violations of MSRB Rules G-18 and G-30 that do not involve a dealer's excessive profit, but do involve unfair pricing based on an inattention to market value. See MSRB Notice 2004-3 (Review of Dealer Pricing Responsibilities) (Jan. 26, 2004).
 - 2 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range. Adjudicators should order restitution or increase the recommended fine amount by adding the amount of a respondent's financial benefit. In cases involving best execution violations that arose from intentional or reckless misconduct, Adjudicators may consider imposing a set fine amount per violation rather than in the aggregate.
 - 3 Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
 - 4 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

ECN Display Rule—Failure to Comply with Rule Requirements

NASD Conduct Rule 2110 and Regulation NMS, Rule 602 [SEC Request 11Ac1-1]

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p>See <u>Principal Considerations in Introductory Section</u></p> <ol style="list-style-type: none"> Whether the priced order was a customer order, rather than an order entered for the account of the market maker. Whether the priced customer order was executed during the period of non-compliance, while other transactions were executed in the marketplace at prices equal to or better than that priced order. Evidence of significant adverse impact on market-price discovery or transparency that occurred because the order was not displayed at all, was displayed only after long delay, or was displayed in a grossly incorrect manner. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p>First Action²⁽¹⁾ Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p>Second Action Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p>Subsequent Actions Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.³</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years or expelling the firm and/or barring the responsible individual.</p>

1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

2[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.

3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Failure to Display Minimum Size in NASDAQ Securities, CQS Securities and OTC Bulletin Board® Securities

NASD Conduct Rule 2110 and Marketplace Rules 4613 and 6750

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p><u>See <i>Principal Considerations in Introductory Section</i></u></p>	<p><i>First Action</i>²⁽¹⁾ Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [5,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u> [25,000].³</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions for up to 20 business days and/or suspending the responsible individual in any or all capacities for up to 20 business days.</p>

1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

2[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.

3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

New Guideline
 Guideline for Fixed Income Pricing System deleted.

Trade Reporting and Compliance Engine (TRACE)—Late Reporting; Failing to Report; False, Inaccurate or Incomplete Reporting

NASD Systems & Programs Rules 6230; Conduct Rule 2110¹

<u>Principal Considerations in Determining Sanctions</u>	<u>Monetary Sanction²</u>	<u>Suspension, Bar, or Other Sanctions</u>
<p><u>See Principal Considerations in Introductory Section³</u></p> <p>Extent to which violative conduct affected market transparency, the dissemination of trade information, or the regulatory audit trail.</p> <p>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</p> <p>Whether respondent violated rule requirements during an extended period of days. (Adjudicators should treat as aggravating the fact that a respondent's failure to report or incorrect reporting occurred for more than one week. Adjudicators should treat as egregious misconduct a respondent's failing to report for several weeks.)</p> <p>Whether a reporting violation was readily apparent from a review of NASD's TRACE website (or MSRB's website for violations of MSRB Rule G-14).⁶</p>	<p><u>For All Types of Violations</u></p> <p><u>First Action⁴</u> Fine of \$5,000 to \$10,000.</p> <p><u>Second Action</u> Fine of \$10,000 to \$50,000.</p> <p><u>Subsequent Actions</u> Fine of \$10,000 to \$100,000.⁵</p> <p>In all egregious cases, whether a first, second, or subsequent action, consider a fine greater than or equal to the high end of the range for a first, second, or subsequent action. Also consider imposing the fine on a "per violation" basis.</p>	<p><u>For All Types of Violations</u></p> <p><u>Firm</u></p> <p>In egregious cases, consider a suspension (of up to two years) or expulsion of the firm.</p> <p><u>Responsible Individual</u></p> <p>Consider suspending the responsible individual in any or all capacities for up to 30 business days.</p> <p>In egregious cases, consider a lengthier suspension (of up to two years) or a bar.</p>

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- 1 This Guideline also is appropriate for violations of MSRB Rule G-14 AND G-17.
 - 2 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.
 - 3 A respondent's delegation of its reporting responsibilities to a third party who caused or contributed to respondent's violation is not an independent basis for mitigation.
 - 4 Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
 - 5 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.
 - 6 In cases in which the respondent does not detect a reporting failure or violation that would have been apparent from a routine review of data such as, for example, transaction reporting cards on NASD's TRACE website or MSRB's website, Adjudicators should consider the respondent's violations to be egregious.

Limit Order Display Rule—Failure to Comply with Rule Requirements

NASD Conduct Rule 2110 and Regulation NMS, Rule 604 [SEC Rule 11Ac1-4]

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p>See <u>Principal Considerations in Introductory Section</u></p> <ol style="list-style-type: none"> Whether customer limit order was executed during the period of non-compliance and whether other transactions were executed at prices equal to or better than that customer limit order. Whether misconduct had a significant adverse impact on market-price discovery or transparency. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p>First Action²⁽¹⁾ Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p>Second Action Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p>Subsequent Actions Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.³</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years or expelling the firm and/or barring the responsible individual.</p>

- 1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.
- 2[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
- 3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Limit Order Protection Rule—Failure to Comply with Rule Requirements

NASD Conduct Rule 2110 And IM 2110-2

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p><u>See <i>Principal Considerations In Introductory Section</i></u></p> <ol style="list-style-type: none"> Whether respondent traded ahead of and/or failed to execute a customer limit order. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p><i>First Action</i>²⁽¹⁾ Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.³</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years.</p>

1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

2[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.

3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Locked/Crossed Market—Failure to Comply with Rule Requirements

NASD Conduct Rule 2110 and Marketplace Rule 4613

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p>See <i>Principal Considerations in Introductory Section</i></p> <ol style="list-style-type: none"> Whether the locked/crossed market affected the market at a particularly sensitive time, such as at the market open, at commencement of secondary trading, or on an expiration date. While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services. 	<p>First Action^{1/2} Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p>Second Action Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p>Subsequent Actions Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.³</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years or expelling the firm and/or barring the responsible individual.</p>

¹ In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

²[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.

³ If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Marking the Close or Open

NASD Conduct Rules 2110 and 3310

Principal Considerations in Determining Sanctions	Monetary Sanction	Suspension, Bar, or Other Sanctions
<p><u>See <i>Principal Considerations In Introductory Section</i></u></p> <ol style="list-style-type: none"> 1. Whether <u>the misconduct resulted in protecting[ed] a securities position or enhancing[ed] size.</u> 2. Whether respondent received a benefit from the misconduct, including but not limited to increased valuation of inventory, avoidance of margin calls, <u>or affecting month-end performance.</u> 3. <u>Whether the activity affected the market at a particularly sensitive time, such as on an expiration date.</u> 4. <u>Whether the misconduct was an isolated incident involving one stock or a systemic pattern of behavior involving multiple stocks.</u> 	<p>Fine of \$25,000 to <u>\$200,000 [100,000].</u></p> <p><u>In egregious cases, consider a fine in excess of \$200,000.</u></p>	<p><i>Negligent Misconduct</i></p> <p>Suspend individual in any or all capacities and/or suspend firm with respect to any or all activities or functions for up to 30 business days.</p> <p><i>Intentional Or Reckless Misconduct</i></p> <p>Suspend individual in any or all capacities and/or suspend firm with respect to any or all activities or functions for up to two years.</p> <p>In egregious cases, consider barring the individual and/or expelling the firm.</p>

Options Exercise and Positions Limits—Failure to Comply with Rule Requirements

NASD Conduct Rules 2110 and 2860

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p><i>See <u>Principal Considerations in Introductory Section</u></i></p>	<p>First Action² Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p>Second Action Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p>Subsequent Actions Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.³</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years or prohibiting the firm from conducting options transactions.</p>

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- 1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range. [As set forth in General Principle No. 6, Adjudicators may increase the recommended fine amount by adding the amount of a respondent's financial benefit.]
 - 2 Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
 - 3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Options Positions Reporting—Late Reporting and Failing to Report

NASD Conduct Rules 2110 and 2860(b)(5)

<u>Principal Considerations in Determining Sanctions¹</u>	<u>Monetary Sanction²</u>	<u>Suspension, Bar, or Other Sanctions</u>
<p>See <i>Principal Considerations in Introductory Section</i></p> <ol style="list-style-type: none"> Size of the positions not reported. [Number of days the positions were not reported.] <u>Whether respondent violated rule requirements during an extended period of days. (Adjudicators should treat as aggravating the fact that a respondent's failure to report or incorrect reporting occurred for more than one week. Adjudicators should treat as egregious misconduct a respondent's failure to report for several weeks.)</u> Evidence of respondent's potential for benefit or monetary gain. 	<p><i>Late Reporting and Failing to Report</i></p> <p>[Late Reporting]</p> <p>[First Action¹ Fine of \$1,000 to \$2,000.]</p> <p>[Second Action Fine of \$2,000 to \$10,000.]</p> <p>[Subsequent Actions Fine of \$ 5,000 to \$25,000.]</p> <p>[Failure of Report]</p> <p><i>First Action³</i> Fine of <u>\$5,000</u> [2,000] to \$10,000.</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> to <u>\$50,000</u>.</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u> [25,000].⁴</p> <p><u>In all egregious cases, whether a first, second, or subsequent action, consider a fine greater than or equal to the high end of the range for a first, second, or subsequent action. Also consider imposing the fine on a "per violation" basis.</u></p>	<p><i>Failure to Report</i></p> <p>In egregious cases, consider suspending the responsible individual in any or all capacities for up to two years or barring the individual. Also consider suspending the firm from conducting options transactions for up to two years or barring the firm from conducting options transactions.</p>

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- 1 A respondent's delegation of its reporting responsibilities to a third party who caused or contributed to respondent's violation is not an independent basis for mitigation.
 - 2 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.
 - 3[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
 - 4 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Order Audit Trail System (OATS)—Late Reporting; Failing to Report; False, Inaccurate or Misleading Reporting; and Clock Synchronization Failure

NASD Systems and Programs Rules 6950 through 6957

Principal Considerations in Determining Sanctions ²	Monetary Sanction ¹
<p><u>See Principal Considerations in Introductory Section</u></p> <ol style="list-style-type: none"> Nature of OATS reporting violation. Extent to which violative conduct affected the regulatory audit trail. <u>Whether violation occurred over an extended period of days.</u> <u>Whether reporting violation was readily apparent from a review of NASD's OATS Website.⁴</u> <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p><u>Late Reporting, Failing to Report, False, Inaccurate or Misleading Reporting</u></p> <p><i>First Action</i>^{3(f)} Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to \$100,000.⁵</p> <p>In all egregious cases, <u>whether a first, second, or subsequent action, consider a fine [of \$10,000 to \$150,000] greater than or equal to the high end of the range for a first, second, or subsequent action.</u></p> <p>[Failure to Report and Inaccurate or Misleading Reporting]</p> <p>[First Action Fine of \$5,000 to \$10,000.]</p> <p>[Subsequent Actions Fine of \$10,000 to \$100,000.]</p> <p>[In egregious cases, fine of \$15,000 to \$150,000.]</p> <p><u>Failure to Synchronize Clocks</u></p> <p><i>First Action</i> Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [5,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to \$50,000.⁵</p>

Suspension, Bar, or Other Sanctions

For All Types of Violations

Firm

Consider suspending the firm with respect to any or all activities or functions for up to 30 business days. In egregious cases, consider a [lengthier] suspension (of up to two years) or expulsion of the firm.

Individual

Subsequent Actions

Consider suspending the responsible individual in any or all capacities for up to 30 business days.

In egregious cases, consider a lengthier suspension (of up to two years) or a bar.

- 1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.
- 2 A respondent's delegation of its reporting responsibilities to a third party who caused or contributed to respondent's violation is not an independent basis for mitigation.
- 3[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
- 4 In cases in which the respondent fails for more than one week to detect a failure to report that would have been apparent from a review of data on the OATS Website, Adjudicators should consider the respondent's violations to be egregious.
- 5 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Passive Market Making Violations

NASD Conduct Rule 2110 and Regulation M

<u>Principal Considerations in Determining Sanctions</u>	<u>Monetary Sanction¹</u>	<u>Suspension, Bar, or Other Sanctions</u>
<p><i>See <u>Principal Considerations in Introductory Section.</u></i></p>	<p><i>First Action</i>²⁽¹⁾ Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u>.³</p>	<p>In egregious cases, consider suspending responsible individual in any or all capacities for up to two years or barring responsible individual. Also consider suspending the firm with respect to any or all activities or functions for up to two years.</p>

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- 1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.
- 2[1] Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.
- 3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Short Sale Violations

Conduct Rules 3350 (Short Sale Rule), 3360 (Short-Interest Reporting), [3370 (Prompt Receipt and Delivery of Securities] Marketplace Rule 6130(d)(6) (Trade Report Input); IM-3350 (Short Sale Rule); and Regulation SHO

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p><u>See <i>Principal Considerations in Introductory Section</i></u></p> <ol style="list-style-type: none"> <li data-bbox="164 730 727 856">1. <u>In cases involving short interest reporting, consider the number of months during which the respondent failed to report short interest or reported short interest incorrectly.⁴</u> <li data-bbox="164 877 727 1381">2. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p><i>First Action</i>² Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p><i>Second Action</i> Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p><i>Subsequent Actions</i> Fine of <u>\$10,000</u> [5,000] to <u>\$100,000.</u>⁵</p> <p><u>In all egregious cases, whether a first, second, or subsequent action, consider a fine greater than or equal to the high end of the range for a first, second, or subsequent action. Also consider imposing the fine on a "per violation" basis.</u></p>	<p>If the short-selling customer is not subject to NASD jurisdiction, in egregious cases or those with evidence of willful misconduct, consider adding the amount of the short-selling customer's "transaction profit"³ to the fine for the executing member and/or associated person. In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible Individual in any or all capacities for up to two years or expelling the firm and/or barring the responsible individual.</p>

1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

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

2 Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time, however, should be given more weight than less recent events.

3 "Transaction profit" means the profit that the short-selling customer realized. This amount is separate and distinct from the respondent's financial benefit, as described in General Principle No. 6.

4 Adjudicators should treat as aggravating the fact that a respondent's failure to report or incorrect reporting of short interest occurred for more than one month. A respondent's delegation of its reporting responsibilities to a third party who caused or contributed to respondent's violation is not an independent basis for mitigation.

5 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Trade Reporting—Late Reporting; Failing to Report; False, Inaccurate or Misleading Reporting

NASD Conduct Rule 2110 and Equity Trade Reporting Rules [Marketplace Rules 4630 through 4652, 6130, 6400 through 6420, 6600 through 6620, and 6700 through 6750¹]

Principal Considerations in Determining Sanctions	Monetary Sanction ¹	Suspension, Bar, or Other Sanctions
<p>See <i>Principal Considerations In Introductory Section</i></p> <ol style="list-style-type: none"> Nature of trade reporting violation. Whether violative conduct affected market-price discovery data. Whether operational problems caused delayed reports. <u>Whether respondent violated rule requirements over an extended period of days.</u> <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p>First Action² Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [2,000].</p> <p>Second Action Fine of <u>\$10,000</u> [2,000] to <u>\$50,000</u> [10,000].</p> <p>Subsequent Actions Fine of <u>\$10,000</u> [5,000] to \$100,000.³</p> <p><u>In all egregious cases, whether a first, second, or subsequent action, consider a fine greater than or equal to the high end of the range for a first, second, or subsequent action.</u></p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending responsible individual in any or all capacities for up to two years.</p> <p>Also consider expelling the firm and/or barring the responsible individual.</p>

1 This guideline also is appropriate for violations of MSRB Rule G-14. In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.

[1]2 Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time should be given more weight than less recent events.

3 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

Prohibition on Transactions, Publication of Quotations or Publication of Indications of Interest [Trades Executed] During Trading Halts

NASD Conduct Rules 2110 And 3340¹

<u>Principal Considerations in Determining Sanctions</u>	<u>Monetary Sanction</u>	<u>Suspension, Bar, or Other Sanctions</u>
<p><u>See <i>Principal Considerations in Introductory Section</i></u></p> <p>1. Whether respondent knew of the trading halt.</p>	<p>Fine of <u>\$5,000</u> [1,000] to <u>\$50,000</u> [10,000].^[2]</p> <p>In egregious cases, <u>consider a fine in excess of \$50,000</u> [10,000-100,000].</p>	<p>In egregious cases, consider suspending the firm with respect to any or all activities or functions and/or suspending the responsible individual in any or all capacities for up to two years or expelling the firm and/or barring the responsible individual.</p>

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- 1 This Guideline also is appropriate for violations of MSRB Rule G-13.
 - [2 As set forth in General Principle No. 6, Adjudicators may increase the recommended fine amount by adding the amount of a respondent's financial benefit.]

Reports of Execution Quality and Order Routing

Regulation NMS, Rules 605 & 606

<u>Principal Considerations in Determining Sanctions</u>	<u>Monetary Sanction¹</u>	<u>Suspension, Bar, or Other Sanctions</u>
<p><u>See Principal Considerations in Introductory Section²</u></p> <ol style="list-style-type: none"> 1. <u>Whether respondent violated rule requirements during a period of months.⁴</u> 2. <u>While respondents are responsible for the systems that they use and the third-party vendors that they employ, the appropriate level of sanctions will depend on whether the respondent diligently chose, installed, and tested a system that nevertheless malfunctioned; the frequency and thoroughness with which the respondent ensured that the system was operating in compliance with applicable rules; and the care that the respondent exercised in undertaking all necessary steps to correct systems-related malfunctions. The same considerations apply to a respondent that has relied on a third-party vendor's products or services.</u> 	<p><u>First Action²</u> <u>Fine of \$10,000 to \$20,000.</u></p> <p><u>Second Action</u> <u>Fine of \$20,000 to \$50,000.</u></p> <p><u>Subsequent Actions</u> <u>Fine of \$20,000 to \$100,000.⁵</u> <u>In all egregious cases, whether a first, second, or subsequent action, consider a fine greater than or equal to the high end of the range for a first, second, or subsequent action. Also consider imposing the fine on a "per violation" basis.</u></p>	

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- 1 In cases in which the violations: (1) involve a pattern or patterns of misconduct; (2) can be quantified by number or percentage; or (3) can be compared to the standard maintained by industry peers, Adjudicators may consider deviating from the fine structure recommended in this guideline for first, second, or subsequent actions. Imposition of monetary sanctions greater than those recommended in this guideline may be particularly appropriate in cases involving violations that occurred during two or more examination or review periods or violations that occurred over an extended period of time. Similarly, in cases in which the respondent acted intentionally or recklessly, and in cases in which the respondent's compliance rate is significantly lower than that of its peers, Adjudicators may impose a monetary sanction in excess of the recommended range.
 - 2 Adjudicators should consider actions concerning violative events that occurred within the three years prior to the misconduct at issue. Events that are more recent in time should be given more weight than less recent events.
 - 3 A respondent's delegation of its reporting responsibilities to a third party who caused or contributed to respondent's violation is not an independent basis for mitigation.
 - 4 Adjudicators should treat as aggravating the fact that a respondent's failure to report or incorrect reporting occurred for more than one month.
 - 5 If respondent's second or subsequent action involves a violation that is less serious than a prior violation, includes conduct that demonstrates that respondent is improving its compliance rate, or involves mitigation that did not exist in a prior action, Adjudicators may consider imposing a fine that is less than the fine imposed in the prior action.

MSRB Rule G-36 (Timely Filing of Offering Documents with the MSRB)— Late Filing and Failing to File

MSRB Rule G-36

Principal Considerations in Determining Sanctions	Monetary Sanction	Suspension, Bar, or Other Sanctions
<p>See <i>Principal Considerations in Introductory Section</i></p> <ol style="list-style-type: none"> Average number of days late. Whether respondent also failed to comply with the recordkeeping requirements of MSRB Rule G-8 concerning the delivery to the MSRB of Official Statements and Advance Refunding Documents. Evidence of improper mailing, i.e., by means that do not provide a record of sending. <u>Extent to which violative conduct deprived the investors or other market participants of publicly available information regarding the issuer.</u> 	<p>Late Filing</p> <p>Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [\$3,000]. <u>Consider imposing a fine on a per violation basis.</u></p> <p>Failure to File</p> <p>Fine of <u>\$5,000</u> [1,000] to <u>\$20,000</u> [5,000]. <u>Consider imposing a fine on a per violation basis.</u></p>	<p>Late Filing</p> <p>In egregious cases, consider suspending the firm from engaging in all municipal underwriting activities for up to 30 business days. Also consider suspending the responsible individual in any or all capacities for up to 30 business days.</p> <p>Failure to File</p> <p>In egregious cases, consider suspending the firm from engaging in all municipal underwriting activities for up to 30 business days. Also consider suspending the responsible individual in any or all capacities for up to 30 business days.</p>

MSRB Rules G-37 [G-38] Reporting—Late Filing; Failing to File; Filing False or Misleading Reports

MSRB Rules G-37 and G-38

Principal Considerations in Determining Sanctions	Monetary Sanction ²	Suspension, Bar, or Other Sanctions
<p>See <i>Principal Considerations in Introductory Section</i></p> <ol style="list-style-type: none"> Whether the report is inaccurate, outdated, or both. Whether respondent is active in the municipal underwriting business and generally makes political contributions. Whether respondent eventually filed report, albeit late. Whether violation involved failing to report political contributions or failing to report participation in an underwriting. <u>Extent to which violative conduct deprived the investing public or other market participants of information regarding the issuer.</u> <u>With respect to false or misleading reports, whether misconduct was intentional or reckless.</u> 	<p>Late Filing</p> <p>Fine of <u>\$5,000</u> [1,000] to <u>\$10,000</u> [\$3,000]. <u>Consider imposing a fine on a per violation basis.</u></p> <p>Failure to File</p> <p>Fine of <u>\$5,000</u> [1,000] to <u>\$20,000</u> [5,000]. <u>Consider imposing a fine on a per violation basis.</u></p> <p>Filing False or Misleading Reports</p> <p>Fine of <u>\$10,000</u> [5,000] to <u>\$100,000</u> per violation.</p>	<p>Late Filing</p> <p>In egregious cases, consider suspending the firm from engaging in all municipal underwriting activities for up to 30 business days. Also consider suspending the responsible individual in any or all capacities for up to 30 business days.</p> <p>Failure to File</p> <p>In egregious cases, consider suspending the firm from engaging in all municipal underwriting activities for up to 30 business days and thereafter until the firm files accurate reports, as required by the rules. Also consider suspending the responsible individual in any or all capacities for up to 30 business days.</p> <p>Filing False or Misleading Reports</p> <p>Consider suspending the firm from engaging in all municipal underwriting activities for up to two years. Also consider suspending the responsible individual in any or all capacities for up to two years or barring the individual.</p>

[NASD Regulation enforces MSRB Rules G-37 and G-38, as interpreted by the MSRB.]

Notice to Members

MARCH 2006

SUGGESTED ROUTING

Legal & Compliance
Operations
Registered Representatives
Senior Management
Training

KEY TOPICS

IM-3013 (Annual Compliance and Supervision Certification)

GUIDANCE

Annual Compliance and Supervision Certification

SEC Approves Amendment to NASD Interpretive Material 3013 Regarding Timing of Submission of Report that Evidences Processes to a Member's Board of Directors and Audit Committee; **Effective Date: March 17, 2006**

Executive Summary

The Securities and Exchange Commission (SEC) has approved an amendment to Interpretive Material 3013 (IM-3013) to establish the timing with respect to the requirement to submit to the member's board of directors and audit committee (or equivalent bodies) a report that evidences certain processes that form the basis of a certification by the Chief Executive Officer (CEO) under Rule 3013.¹ The rule change permits submission of the final report to these governing bodies to take place either before or after the execution of the certification, provided that the board of directors and audit committee (or equivalent bodies) receive the report at the earlier of their next scheduled meetings or within 45 days after execution of the certification. The rule change became effective upon SEC approval on March 17, 2006.

The text of IM-3013 with the changes indicated is in Attachment A.

Questions/Further Information

Questions concerning this *Notice* may be directed to Philip Shaikun, Associate Vice President and Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8451.

Background and Discussion

NASD Rule 3013 requires each member's CEO or equivalent officer to certify annually that the member has in place processes to establish, maintain, review, modify and test policies and procedures reasonably designed to achieve compliance with applicable NASD rules, MSRB rules and the federal securities laws. The rule is accompanied by IM-3013, which sets forth the actual certification language and also provides additional guidance about the requirements of the rule and sets forth certain limitations to its scope.

The certification consists of four attestations, each set forth in a separate numbered paragraph within IM-3013. In paragraph 3 of the certification, the CEO attests that the member's processes are "evidenced in a report reviewed by the chief executive officer (or equivalent officer), chief compliance officer, and such other officers as the Member may deem necessary to make this certification, and submitted to the Member's board of directors and audit committee."

The rule is not intended to require the board of directors or audit committee to review or consider the report as a condition to the CEO executing the certification. Rather, the requirement that the report be submitted to the member's board of directors and audit committee (or equivalent bodies) is intended to ensure that those governing bodies remain informed of this aspect of the member's compliance system in the context of their overall responsibility for governance and internal controls of the member for which they serve. Accordingly, the rule change permits submission of the final report to these governing bodies to take place either before or after the execution of the certification, provided that the board of directors and audit committee (or equivalent bodies) receive the report at the earlier of their next scheduled meetings or within 45 days after execution of the certification. Importantly, the board of directors and audit committee (or equivalent bodies) must receive the report in its final form regardless of whether the member elects to submit it to them before or after certification by the CEO.

The rule change became effective upon SEC approval on March 17, 2006. Members must execute their first CEO certification no later than April 1, 2006.

Endnote

- 1 Exchange Act Release No. 53509 (March 17, 2006) (SR-NASD-2006-036).

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ATTACHMENT A

Text of approved rule change. New language is underlined; deletions are in double brackets.

IM-3013. Annual Compliance and Supervision Certification

The NASD Board of Governors is issuing this interpretation to the requirement under Rule 3013(b), which requires that the member's chief executive officer (or equivalent officer) execute annually¹ a certification that the member has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable NASD rules, MSRB rules and federal securities laws and regulations. The certification shall state the following:

* * * * *

Annual Compliance and Supervision Certification

The undersigned is the chief executive officer (or equivalent officer) of [name of member corporation/partnership/sole proprietorship] (the "Member"). As required by NASD Rule 3013(b), the undersigned makes the following certification:

1. The Member has in place processes to:

(a) establish, maintain and review policies and procedures reasonably designed to achieve compliance with applicable NASD rules, MSRB rules and federal securities laws and regulations;

(b) modify such policies and procedures as business, regulatory and legislative changes and events dictate; and

(c) test the effectiveness of such policies and procedures on a periodic basis, the timing and extent of which is reasonably designed to ensure continuing compliance with NASD rules, MSRB rules and federal securities laws and regulations.

2. The undersigned chief executive officer (or equivalent officer) has conducted one or more meetings with the chief compliance officer in the preceding 12 months, the subject of which satisfy the obligations set forth in IM-3013.

3. The Member's processes, with respect to paragraph 1 above, are evidenced in a report reviewed by the chief executive officer (or equivalent officer), chief compliance officer, and such other officers as the Member may deem necessary to make this certification [[, and]]. The final report has been submitted to the Member's board of directors and audit committee or will be submitted to the Member's board of directors and audit committee (or equivalent bodies) at the earlier of their next scheduled meetings or within 45 days of the date of execution of this certification.

4. The undersigned chief executive officer (or equivalent officer) has consulted with the chief compliance officer and other officers as applicable (referenced in paragraph 3 above) and such other employees, outside consultants, lawyers and accountants, to the extent deemed appropriate, in order to attest to the statements made in this certification.²

* * * * *

It is critical that each NASD member understand the importance of employing comprehensive and effective compliance policies and written supervisory procedures. Compliance with applicable NASD rules, MSRB rules and federal securities laws and regulations is the foundation of ensuring investor protection and market integrity and is essential to the efficacy of self-regulation. Consequently, the certification requirement is intended to require processes by each member to establish, maintain, review, test and modify its compliance policies and written supervisory procedures in light of the nature of its businesses and the laws and rules that are applicable thereto, and to evidence such processes in a report reviewed by the chief executive officer (or equivalent officer) executing the certification.

Included in this processes requirement is an obligation on the part of the member to conduct one or more meetings annually between the chief executive officer (or equivalent officer) and the chief compliance officer to: (1) discuss and review the matters that are the subject of the certification; (2) discuss and review the member's compliance efforts as of the date of such meetings; and (3) identify and address significant compliance problems and plans for emerging business areas.

The periodic and content requirements for meetings between the chief executive officer (or equivalent officer) and the chief compliance officer, as well as the pertinent requirements of paragraphs 3 and 4 of the certification, are intended to indicate the unique and integral role of the chief compliance officer both in the discharge of certain compliance processes and reporting requirements that are the subject matter of the certification and in providing a reliable basis upon which the chief executive officer can execute the certification. The chief compliance officer is the primary advisor to the member on its overall compliance scheme and the particularized rules, policies and procedures that the member adopts. This is because the chief compliance officer should have an

expertise in the process of (1) gaining an understanding of the products, services or line functions that need to be the subject of written compliance policies and written supervisory procedures; (2) identifying the relevant rules, regulations, laws and standards of conduct pertaining to such products, services or line functions based on experience and/or consultation with those persons who have a technical expertise in such areas of the member's business; (3) developing, or advising other business persons charged with the obligation to develop, policies and procedures that are reasonably designed to achieve compliance with those relevant rules, regulations, laws and standards of conduct; (4) evidencing the supervision by the line managers who are responsible for the execution of compliance policies; and (5) developing programs to test compliance with the member's policies and procedures.

It is that expertise in the process of compliance that makes the chief compliance officer an indispensable party to enable the chief executive officer to reach the conclusions stated in the certification. Consequently, any certification made by a chief executive officer under circumstances where the chief compliance officer has concluded, after consultation, that there is an inadequate basis for making such certification would be, without limitation, conduct inconsistent with the observance of the high standards of commercial honor and the just and equitable principles of trade - a violation of Rule 2110. Beyond the certification requirement, it is the intention of both Rule 3013 and this Interpretive Material to foster regular and significant interaction between senior management and the chief compliance officer regarding the member's comprehensive compliance program.

The chief compliance officer and other compliance officers that report to the chief compliance officer (as described in the sentence that immediately follows) shall perform the compliance functions contemplated by this Interpretive Material and paragraphs 3 and 4 of the certification. Nothing in this Interpretive Material is intended to limit or discourage the participation of other employees both within and without the member's compliance department in any aspect of the member's compliance programs or processes, including those matters discussed in this Interpretive Material. However, it is understood that the chief compliance officer and, where applicable, the most senior compliance officers having primary compliance department responsibility for each of the member's business segments, will retain responsibility for the compliance functions contemplated by this Interpretive Material and paragraphs 3 and 4 of the certification.

As may be necessary to render their views and advice, the chief compliance officer and the other officers referenced in paragraph 3 of the certification who consult with the chief executive officer (or equivalent officer) pursuant to paragraph 4, shall, in turn, consult with other employees, officers, outside consultants, lawyers and accountants.

The NASD Board of Governors recognizes that supervisors with business line responsibility are accountable for the discharge of a member's compliance policies and written supervisory procedures. The signatory to the certification is certifying only as to having processes in place to establish, maintain, review, test and modify the member's written compliance and supervisory policies and procedures and the execution of this certification and any consultation rendered in connection with such certification does not by itself establish business line responsibility.

The requirement to designate a chief compliance officer does not preclude such person from holding any other position within the member, including the position of chief executive officer, provided that such person can discharge the duties of a chief compliance officer in light of his or her other additional responsibilities. The requirement that a member's processes include providing the report to the board of directors and audit committee (required by paragraph 3 of the certification) does not apply to members that do not utilize these types of governing bodies and committees in the conduct of their business.³

The report required in paragraph 3 of the certification must document the member's processes for establishing, maintaining, reviewing, testing and modifying compliance policies, that are reasonably designed to achieve compliance with applicable NASD rules, MSRB rules and federal securities laws and regulations, and any principal designated by the member may prepare the report. The report must be produced prior to execution of the certification and be reviewed by the chief executive officer (or equivalent officer), chief compliance officer and any other officers the member deems necessary to make the certification and must be provided to the member's board of directors and audit committee in final form either prior to execution of the certification or at the earlier of their next scheduled meetings or within 45 days of execution of the certification. The report should include the manner and frequency in which the processes are administered, as well as the identification of officers and supervisors who have responsibility for such administration. The report need not contain any conclusions produced as a result of following the processes set forth therein. The report may be combined with any other compliance report or other similar report required by any other self-regulatory organization provided that (1) such report is clearly titled in a manner indicating that it is responsive to the requirements of the certification and this Interpretive Material; (2) a member that submits a report for review in response to an NASD request must submit the report in its entirety; and (3) the member makes such report in a timely manner, i.e., annually.

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- 1 Members must ensure that each ensuing annual certification is effected no later than on the anniversary date of the previous year's certification.
 - 2 Members should understand that the requirements of Rule 3013 and this Interpretive Material represent, in part, a principle-based requirement to certify that the member has in place processes to establish, maintain, review, test and modify written compliance policies and written supervisory procedures reasonably designed to achieve compliance with applicable NASD rules, MSRB rules and federal securities laws and regulations. Consequently, compliance with the periodic and content requirements in this Interpretive Material pertaining to meetings between the chief executive officer (or equivalent officer) and the chief compliance officer does not satisfy the full extent of these principle-based obligations that will vary with the facts and circumstances of a member's business activities and organizational structure. Moreover, NASD emphasizes the testing aspect of this principle-based requirement; an integral purpose of NASD rules pertaining to supervision is that members adopt policies and procedures that are effective as to both the scope of, and the achievement of compliance with, applicable NASD rules, MSRB rules and federal securities laws and regulations.
 - 3 As a part of their process, members must have the report reviewed by their governing bodies and committees that serve similar functions in lieu of a board of directors and audit committee.

Notice to Members

MARCH 2006

SUGGESTED ROUTING

Senior Management
Continuing Education
Legal & Compliance
Operations
Registered Representatives
Registration
Training

KEY TOPICS

Branch Office Definition
Branch Office Registration
Central Registration Depository (CRD® or Web CRD)
Form BR (Uniform Branch Office Registration Form)
IM-3010-1
Internal Inspections
Rule 3010
Supervision

GUIDANCE

Uniform Branch Office Definition

Extension of Effective Date of NASD Uniform Branch Office Definition and Certain Form BR and Form U4 Filing Requirements from May 1, 2006 to July 3, 2006

Joint Interpretive Guidance from NASD and the NYSE Relating to Uniform Branch Office Definition Under NASD Rule 3010(g)(2) and NYSE Rule 342.10

Effective Date of Uniform Definition:

NASD: July 3, 2006; NYSE: September 9, 2005

Executive Summary

On September 9, 2005, the Securities and Exchange Commission (SEC) approved (1) amendments to NASD Rule 3010(g)(2) to revise the definition of "branch office"; and (2) adoption of IM-3010-1 to provide guidelines on factors to be considered by a member in conducting internal inspections of offices (Uniform Definition).¹ The SEC simultaneously approved amendments to the New York Stock Exchange, Inc.'s (NYSE) Rule 342 (Offices – Approval, Supervision and Control) to provide a new, uniform industry definition of the term "branch office."²

The NYSE's Uniform Definition became effective on September 9, 2005. A copy of the amended rule text is attached hereto as Attachment A (NASD) and Attachment B (NYSE).

NASD has filed for immediate effectiveness an extension to July 3, 2006 of (1) the Uniform Definition; and (2) the transition deadline for compliance with Form BR (Uniform Branch Office Registration Form) and Form U4 (Uniform Application for Securities Industry Registration or Transfer) filing requirements for firms with respect to those branch offices of a firm in existence before the close of business on October 14, 2005.³ The rule change became effective on its March 14, 2006 filing date.⁴

06-12

On September 30, 2005, the SEC approved new Form BR, which replaced Schedule E of Form BD, the NYSE Branch Office Application Form, and certain state branch office forms.⁵ Form BR became effective on October 31, 2005.

The Uniform Definition contains several express exemptions from the branch office registration requirements. NASD and the NYSE (the SROs) believe these exemptions make practical sense without compromising investor protection. The SROs are issuing this Joint Interpretive Notice to address certain questions that have arisen regarding the application of these exemptions.

Questions/Further Information

Questions concerning this Joint Interpretive Notice may be directed as follows:

NASD: Chip Jones, Vice President, Registration and Disclosure, at (240) 386-4797, Richard E. Pullano, Associate Vice President/Chief Counsel, Registration and Disclosure, at (240) 386-4821; or Kosha K. Dalal, Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-6903.

NYSE: Stephen Kasprzak, Principal Counsel, Rule and Interpretive Standards, at (212) 656-5226.

Extension of NASD Effective Date

NASD has extended from May 1, 2006 to July 3, 2006 (1) the effective date of the Uniform Definition; and (2) the transition deadline for compliance with Form BR (Uniform Branch Office Registration Form) and Form U4 (Uniform Application for Securities Industry Registration or Transfer) filing requirements for firms with respect to those branch offices of a firm in existence before the close of business on October 14, 2005. Firms will have until July 3, 2006 to (1) complete and file the "conversion" Form BR for each such branch; and (2) with respect to the registered persons employed by such branches, amend all applicable Forms U4 to assign these registered persons to the branch office(s) (or other locations) from which they work.⁶

Numerous members have requested an extension of the May 1, 2006 deadlines as the process for transitioning existing and new branch offices into the new centralized branch office registration system on CRD[®] has been more time consuming than originally anticipated. As a result, NASD believes this one-time extension of the deadlines until July 3, 2006 will allow for a more orderly transition by members to the new Uniform Definition and the new centralized branch office registration system on CRD.

Interpretive Questions

A “branch office” is generally defined as any location where one or more associated persons of a member⁷ regularly conducts the business of effecting any transactions in, or inducing or attempting to induce the purchase or sale of any security, or that is held out as such.

The Uniform Definition excludes from registration as a branch office: (1) a non-sales location that provides customer service or back office functions; (2) an associated person’s primary residence provided it is not held out to the public as a branch office and certain other conditions are satisfied; (3) a location, other than the primary residence, that is used for less than 30 business days in any calendar year for securities business, is not held out to the public as an office, and which satisfies certain of the conditions set forth in the primary residence exemption; (4) a location of convenience used occasionally and by appointment; (5) a location used primarily for non-securities business and from which no more than 25 securities transactions are effected annually; (6) the floor of a registered securities exchange; and (7) a temporary location used as part of a business continuity plan.

The SROs have received questions from broker-dealers and associated persons requesting clarification of certain exemptions under the Uniform Definition. These questions, and SRO responses, are as follows:

“Regularly Conducts the Business of Effecting Transactions”

Q1 The Uniform Definition provides that a “branch office” is “any location where one or more associated persons of a member regularly conducts the business of effecting transactions in, or inducing or attempting to induce the purchase or sale of any security, or is held out as such.” What types of activities would this include?

A1 Such activities would include, for example: (1) soliciting new accounts or orders; (2) opening new accounts; (3) accepting or executing orders; or (4) making recommendations with respect to securities transactions. NASD members should keep in mind that certain activities, such as order execution, may also require a location to be registered as an office of supervisory jurisdiction (OSJ) under NASD Rule 3010(g)(1).

Non-Sales Location/Back Office Exemption

Q2 What types of activities at a location are considered “non-sales locations/customer services/back office” functions for purposes of NASD Rule 3010(g)(2)(A)(i) and NYSE Rule 342.10(A)?

A2 In general, to be exempt from registration as a branch office under these provisions, such locations must be established solely for customer service and/or back office functions and may not be held out to the public as a branch office. No sales activities may be conducted from a non-sales location, which is to say that associated persons conducting business on behalf of a member from such locations may not recommend the purchase or sale of securities, or otherwise communicate with the public for the purpose of accepting orders for the purchase or sale of securities or for executing such orders. Communications with the public solely in a clerical and/or ministerial capacity is permissible under this exemption.

Q3 Can an office established for the sole purpose of soliciting investment-banking services to potential clients be considered a “non-sales” location?

A3 If a location is utilized to solicit a member’s investment banking services, but such investment banking services are not performed from the location, registration as a branch office is not required, provided, of course, no other activities at the location would otherwise require branch office registration. A location from which such investment banking services are performed would require registration.

As defined in NASD Rule 2711 and NYSE Rule 472.20, “investment banking services” include, without limitation, acting as an underwriter in an offering for the issuer, acting as a financial adviser in a merger or acquisition; providing venture capital, equity lines of credit, PIPEs (private investment, public equity transaction), or similar investments; or serving as placement agent for the issuer. The term also includes acting as a member of a selling group in a securities underwriting.⁸

Q4 Can an office engaging solely in proprietary trading or securities lending be considered a “non-sales” location?

A4 An office that engages solely in proprietary trading or securities lending may be considered a “non-sales” location, provided no other sales functions are conducted and the location is not held out to the public as a branch office.

Q5 Can an office where a member stations a NYSE Series 16 qualified supervisory analyst solely to review research reports be considered a “non-sales” location?

A5 The NYSE has provided interpretive guidance⁹ regarding the Uniform Definition for members registered with the NYSE, which provides that a location where a member stations a Series 16 qualified supervisory analyst in an office solely to review research reports is an example of a “non-sales” location. NASD members are advised to consult NASD Rule 3010(g)(1), which provides that such locations may be OSJs if, among other things, final approval of advertising or sales literature for use by persons associated with the member pursuant to Rule 2210(b)(1) occurs at such location. OSJs are required to register as branch offices. If the review of the research reports conducted from such location constitutes something less than final approval and final approval occurs at another location, then a firm may view such location as exempt from branch office registration, provided no other activities at such location would require branch office registration.

Primary Residences

The Uniform Definition exempts from the definition of “branch office” any location that is an associated person’s primary residence¹⁰, provided that: (a) only one associated person, or multiple associated persons who reside at the location and are members of the same immediate family, conduct business from the location; (b) the location is not held out to the public as an office and the associated person does not meet with customers at the location; (c) neither customer funds nor securities are handled at the location; (d) the associated person is assigned to a designated branch office, and such designated branch office is reflected on all business cards, stationery, advertisements, and other communications to the public by the associated person; (e) the associated person’s correspondence and communications with the public are subject to the member’s supervision in accordance with NASD Rule 3010 and NYSE Rules 342 and 472; (f) electronic communications (e.g., email) are transmitted through the member’s electronic system; (g) all orders are entered through the designated branch office or through an electronic system established by the member that is reviewable at the branch office; (h) written supervisory procedures pertaining to supervision of sales activities conducted at the residence are maintained by the member; and (i) a list of the residence locations is maintained by the member.

- Q6 One of the conditions that must be satisfied for the “primary residence” exemption from the Uniform Definition to apply is that the associated person be assigned to a designated branch office, and that the address of such designated branch office be reflected on all business cards, stationery, advertisements and other communications to the public.¹¹ Can an associated person use the unregistered location address in telephone directories, business cards, stationery, advertising or sales literature, so long as such communication also sets forth the address and telephone number of the branch office or OSJ from which the associated person is supervised?
- A6 No. The use of the primary residence address in a telephone directory, business card, stationery, advertising or sales literature will be deemed “holding out” the location as a branch office in violation of NASD Rule 3010(g)(2)(A)(ii)(b) and NYSE Rule 342.10(B)(ii), even if such communication also sets forth the address and telephone number of the branch office or OSJ from which the associated person is supervised.
- Q7 Can an associated person use an unregistered location (e.g., primary residence) telephone number or mobile telephone number in telephone directories, business cards, stationery, advertisements and other communications with the public by such associated person?
- A7 Yes. An associated person can use the telephone number of an unregistered location or a mobile telephone number in telephone directories, business cards, stationery, advertising or other communications with the public, provided (1) the address of the unregistered location is not listed on any such communication; and (2) the communication also includes the telephone number and address of the branch office or OSJ from which the associated person is supervised.

Q8 One of the conditions that must be satisfied for the “primary residence” exemption from the Uniform Definition to apply is that “neither customer funds nor securities are handled at that location.”¹² Are there instances when an associated person may accept funds and/or securities and not violate this condition?

A8 Associated persons may not directly accept funds or securities at their primary residence since this would violate the “primary residence” exemption prohibition against meeting with customers at the residence. Likewise, accepting funds or securities mailed directly to the primary residence address would violate the prohibition against “holding out” the location as a branch office.

However, an associated person working from a primary residence may accept funds or securities at an “office of convenience,”¹³ provided the following conditions are met: (1) the funds are made payable to the member or the issuer, as the case may be; (2) the funds are not deposited by the associated person; and (3) the associated person promptly forwards such funds or securities received from the customer to the member or the issuer, as the case may be.

If an associated person subsequently brings funds and/or securities received from a customer to the primary residence location, it will not be considered a violation of the primary residence exemption provided such funds or securities are promptly forwarded to the member or issuer. However, the associated person must not exercise control over the funds or securities. Members are advised to consider the requirements of SEC Rules 15c3-1 (Net Capital Requirements for Brokers and Dealers) and 15c3-3 (Customer Protection – Reserves and Custody of Securities).¹⁴

Q9 One of the conditions that must be satisfied in order for the “primary residence” exemption to the Uniform Definition to apply is that electronic communications (e.g., email) are transmitted through the member’s electronic systems.¹⁵ Further, such communications must be entered through the designated branch office or through an electronic system established by the member that is reviewable at the branch office.¹⁶ Can an associated person use his or her personal email accounts to communicate with potential or existing customers?

A9 No. All electronic communications must be made through the member’s electronic system, and all orders must be entered through the designated branch office or through an electronic system established by the member that is reviewable at the branch office. In addition, the SEC’s Books and Records Rules (SEC Rules 17a-3 and 17a-4)¹⁷ require members to maintain records of electronic mail communications.

Locations Other than Primary Residences

The Uniform Definition exempts from branch office registration any location, other than primary residences, provided it is used for securities-related activities less than 30-business days in any calendar year.¹⁸ These would generally include vacation or second homes and other non-primary residences. Such locations are subject to most of the criteria (enumerated above) imposed upon exempted primary residences.

In the context of this exemption, the term “business day” is defined to exclude any partial day, provided the associated person spends at least four hours of such business day at his or her designated branch office during the time period such office is normally open for business. This is intended to prevent associated persons from regularly conducting business from locations other than their primary residences for the majority of a business day, without such activity being counted towards the 30-business day limit.

Q10 If a member relies on the “30-business days in one calendar year” exemption, what types of records must a member maintain to demonstrate compliance with the “business day” limitation?

A10 A member is expected to demonstrate compliance with the “business day” limitation by maintaining, at a minimum, logs identifying any such locations, “business days” spent at such locations, and the activities of the associated person conducted from such locations.

Q11 If a member relies on the “30-business days in one calendar year” exemption and the location later exceeds the 30-business day threshold in one calendar year, must the member register the location?

A11 The member’s initial reliance on this exemption must be reasonably determined based on an understanding of the use of such location. Once the 30-business days in a calendar year limit has been reached, members will have a 30 calendar-day window to register such location as a branch office.

Offices of Convenience

The Uniform Definition exempts from branch office registration “offices of convenience.”¹⁹ An office of convenience is defined as a location where an associated person occasionally and exclusively by appointment meets with customers, provided such location is not held out to the public as an office. Where such office of convenience is located on bank premises, signage necessary to comply with applicable federal and state laws, rules and regulations and applicable rules and regulations of the NYSE, other self-regulatory organizations, and securities and banking regulators may be displayed and will not be deemed “holding out” for purposes of this section. NYSE Rule 342(D) prescribes that only signage required by the Interagency Statement (Statement on Retail Sales of Nondeposit Investment Products required under Banking Regulations) may be displayed at such locations. Such limited signage is allowed to prevent confusion on the part of customers who might otherwise believe that only traditional, insured bank-related investments are being offered at the location.

Q12 If an associated person works from multiple offices, (e.g., “bank circuit riders”), can a member rely on the “office of convenience” exemption to not register such locations?

A12 Yes. A member may rely on this exemption to not register multiple locations that an associated person is assigned to, provided: the associated person meets with customers only occasionally and exclusively by appointment at any such location; and no other activities occur at such location that would require branch office registration. For instance, the location may not be held out to the public, other than, in the case of a location on bank premises, displaying signage necessary to comply with applicable federal and state laws, rules and regulations and applicable rules and regulations of other self-regulatory organizations, and securities and banking regulators. The associated person, however, must be assigned to at least one registered location for supervisory purposes. The exemption is not limited to bank locations. Any broker-dealer can use the exemption so long as the conditions of the exemption are satisfied.

Q13 What is the meaning of “occasionally” for purposes of “offices of convenience” exemption pursuant to NASD Rule 3010(g)(2)(A)(iv) and NYSE Rule 342.10(D)?

A13 An associated person may meet with customers at such location by appointment only; however, an associated person may not establish regular business hours at such location or hold out the location in any way (except for signage permitted at banks as discussed above). If customers or prospective customers know that an associated person can be met with regularly (or on some predetermined schedule such as the first Monday of every month) at a particular location, it would not qualify as an office of convenience. If the associated person meets with walk-in customers at such location, such location would not qualify as an office of convenience. For example, if a member has a location in a hospital, school or similar type location where an associated person(s) offers securities (such as through 403(b) type plans²⁰) and the associated person(s) is there on a regular schedule, such location would not qualify for this exemption.

Q14 Can a member provide computer terminals at an office of convenience that allows Internet access by customers to their accounts?

A14 Yes. A member may provide computer terminals at an office of convenience for the limited purposes of allowing customers to: (1) review online, publicly available materials concerning financial and business information such as market quotations, economic indicators, and annual and quarterly reports on companies; (2) make independent investment decisions to buy or sell securities for their own accounts; (3) access their accounts; and (4) enter orders through an order entry and execution system. There can be no publicly displayed signage on the computer terminals (other than permitted bank signage) or other indicia of holding out.

Location Used Primarily to Engage in Non-Securities Transactions

The Uniform Definition exempts from branch office registration locations where associated persons are primarily engaged in non-securities activities (e.g., insurance sales) and from which an associated person effects no more than 25 securities transactions in a calendar year, provided that advertisements or sales literature, including business cards, identifying such location also set forth the locations from which the associated person or persons are directly supervised.²¹

Q15 If a member relies on the non-securities transaction exemption and the location later exceeds the 25 securities transactions in a calendar year limitation, must the member register the location?

A15 A member's initial reliance on this exemption must be reasonably determined based on the use of such location (i.e., an ongoing determination must be made to determine whether the total number of securities transactions effected from the location exceeds the 25-transaction de minimis standard). Once the 25 securities transactions in a calendar year threshold is exceeded, members will be given a 30 calendar-day window to register such locations as branch offices.

Q16 Are there any transactions that do not count towards the "25 securities transactions in a calendar year" limitation?

A16 Yes. Transactions made pursuant to automatic investment plans wherein a customer provides prior written instructions to purchase a predetermined number of shares on a regular basis would not count towards the 25 transactions in one calendar year limitation, provided there is no new recommendation given by an associated person to the customer with respect to such transactions.

Temporary Location Used as Part of a Business Continuity Plan

The Uniform Definition exempts from branch office registration any temporary location established in response to the implementation of a business continuity plan.²²

Q17 If a member begins to use a temporary location as part of its business continuity plan, must it amend the Form BR for this branch office to reflect this temporary location address?

A17 No. The member should continue to use the permanent office address and telephone number if the new location is only a temporary location being used as part of a business continuity plan. If such temporary location becomes permanent, then the member must amend the Form BR for such location to reflect the new address.

Calendar Year

Q18 What is the meaning of the term “calendar year” as used in the Uniform Definition?

A18 The term “calendar year” means the period commencing January 1 and ending December 31.

Call Centers

Q19 If a member operates a call center to respond to customer questions and accept orders at the direction of the customer, without providing any advice or recommendations, must such location be a registered branch office?

A19 Yes. A call center where a member communicates with customers and enters customer orders would qualify as a branch office under NASD Rule 3010(g)(2) and NYSE Rule 342.10. Members should keep in mind that certain activities, such as order execution, may also require a location to be registered as an OSJ under NASD Rule 3010(g)(1) and NYSE Rule 342.10. See also Questions #1 and #2.

Main Offices

Q20 Must a member register its main office as a branch office?

A20 A member must register its main office as a branch office if the activities at such location satisfy the definition of “branch office.”²³

Offices That Supervise Other Offices

NASD Rule 3010(g)(2)(B) and NYSE Rule 342.10 provide that notwithstanding the exclusions provided in 3010(g)(2)(A)(i)-(vii) or 342.10(A)-(G), respectively, any location that is responsible for supervising the activities of persons associated with the member at one or more *non-branch* locations of the member is considered to be a branch office. For example, if an associated person supervises the activities of persons at one or more *non-branch* locations from his primary residence, such primary residence location must be registered as a branch office.

Q21 What is the effective date of this provision?

A21 NASD Rule 3010(g)(2)(B) became effective on January 31, 2005 as part of the Supervisory Controls Amendments.²⁴ The similar provision in NYSE Rule 342.10 became effective on September 9, 2005.

Foreign Offices

Q22 Are foreign offices subject to registration as branch offices?

A22 Yes. Members must register any foreign office that satisfies the definition of “branch office.”

NASD Rule 1017 and Safe Harbor Implications (For NASD Members Only)

Q23 Will a member be required to submit an application pursuant to NASD Rule 1017 if such member has an increase in the number of branch offices?

A23 NASD Rule 1017 requires that a member file an application with NASD for specified changes in ownership or control, or any "material change in business operations as defined in Rule 1011." NASD IM-1011-1 creates a safe harbor for certain changes that are presumed not to be a "material change in business operations," and therefore do not require a member to submit an application pursuant to NASD Rule 1017.

As a result of amended NASD Rule 3010, many members may now be required to register existing office locations as branch offices. Registering an office *existing at or prior to the time of the effective date of the Uniform Definition* will not, in and of itself, be considered a material change in business for purposes of NASD Rule 1017, as no increase or change in the number of offices is taking place due to the registration. Similarly, those existing offices that become branches pursuant to the amended rule will not create any new impact to a member's safe harbor expansion allowance, as the safe harbor provision already contemplates both registered and unregistered offices.²⁵ Additionally, any member that is currently operating pursuant to a membership agreement that contains a restriction on business expansions will be able to register those existing office locations as branch locations, if required, without violating that restriction, as the number of offices to which a member is restricted already includes registered and unregistered offices.

Members are cautioned that, while the mere registration of an existing office as a branch office will not trigger a NASD Rule 1017 filing requirement, the addition and registration of new branches may constitute a material change in business, depending on facts and circumstances, and require NASD approval through the membership application process. Members are encouraged to consult with their respective district offices if they are uncertain of their filing obligations.

Endnotes

- 1 See Exchange Act Release No. 52403 (September 9, 2005); 70 FR 54782 (September 16, 2005); File No. SR-NASD-2003-104 (Order Granting Approval of Proposed Rule Change Relating to Proposed Uniform Branch Office Definition) (SEC Approval Order). See also *NASD Notice to Members 05-67* (October 2005).
- 2 See Exchange Act Release No. 52402 (September 9, 2005); 70 FR 54788 (September 16, 2005); File No. SR-NYSE-2002-34 (Order Granting Approval of Proposed Rule Change Relating to Proposed Uniform Branch Office Definition) (SEC NYSE Approval Order). See also *NYSE Information Memo 05-74* dated October 6, 2005.
- 3 See SR-NASD-2006-037 (March 14, 2006).
- 4 See SR-NASD-2006-037 (March 14, 2006).
- 5 See Exchange Act Release No. 52544 (September 30, 2005); 70 FR 58764 (October 7, 2005); File No. SR-NASD-2005-030 (Order Granting Approval of Proposed Rule Change Relating to Proposed Form BR (Uniform Branch Office Registration Form) and Conforming Changes and Technical Revisions to Form U4 and Form U5). See also Exchange Act Release No. 52543 (September 30, 2005); 70 FR 58771 (October 7, 2005); File No. SR-NYSE-2005-13. See also *NASD Notice to Members 05-66* (October 2005).
- 6 See SR-NASD-2006-037 (March 14, 2006).
- 7 For purposes of this Joint Interpretive Notice, the term "member" refers to NASD members and NYSE member organizations.
- 8 See *NASD Notice to Members 02-39* (July 2002); *NYSE Information Memo 02-26* dated June 26, 2002.
- 9 See *NYSE Information Memo 05-74* dated October 6, 2005.
- 10 NASD Rule 3010(g)(2)(A)(ii) and NYSE Rule 342.10(B).
- 11 NASD Rule 3010(g)(2)(A)(ii)(d) and NYSE Rule 342.10(B)(iv).
- 12 NASD Rule 3010(g)(2)(A)(ii)(c) and NYSE Rule 342.10(B)(iii).
- 13 See NASD Rule 3010(g)(2)(A)(iv) and NYSE Rule 342.10(D).
- 14 See 17 CFR 240.15c3-1 and 15c3-3. See also *NASD Notice to Members 93-30* (NASD Provides SEC-Approved Clarifications and Interpretations to Recent Net Capital Rule Amendments).
- 15 NASD Rule 3010(g)(2)(A)(ii)(f) and NYSE Rule 342.10(B)(vi).
- 16 NASD Rule 3010(g)(2)(A)(ii)(g) and NYSE Rule 342.10(B)(vii).
- 17 See 17 CFR 240.17a-3 and 17a-4.
- 18 NASD Rule 3010(g)(2)(A)(iii) and NYSE Rule 342.10(C).
- 19 NASD Rule 3010(g)(2)(A)(iv) and NYSE Rule 342.10(D).
- 20 Internal Revenue Code Section 403(b).
- 21 NASD Rule 3010(g)(2)(A)(v) and NYSE Rule 342.10(E).
- 22 NASD Rule 3010(g)(2)(A)(vii) and NYSE Rule 342.10(G). For additional information on business continuity plans, see NASD Rules 3510 (Business Continuity Plans) and 3520 (Emergency Contact Information). See also *NASD Notice to Members 04-37* (SEC Approves Rules Requiring Members to Create Business Continuity Plans and Provide Emergency Contact Information) (May 2004). See also NYSE Rule 446 (Business Continuity and Contingency Plans) and *NYSE Information Memos* No. 04-24 dated May 3, 2004; No. 05-63 dated September 2, 2005; No. 05-71 dated September 23, 2005; and No. 05-80 dated October 13, 2005.

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- 23 Adoption of NASD's Uniform Definition supercedes any earlier statements made concerning the registration requirements applicable to members' main offices under NASD rules. NASD notes that IM-1000-4 addresses the need for members to keep their membership applications current, as well as to properly designate and register OSJs and branch offices. NASD intends to propose future amendments to IM-1000-4 to reflect the SEC's approval of the Uniform Definition and new Form BR.
- 24 See Exchange Act Release No. 498832 (June 17, 2004); 69 FR 35092 (June 23, 2004); SR.NASD-2002-162. See also *NASD Notice to Members 05-08* (January 2005). See also Exchange Act Release No. 49882 (June 17, 2004); 69 FR 35108 (June 23, 2004); SR-NYSE-2002-36.
- 25 See NASD IM-1011-1.

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ATTACHMENT A—NASD RULE

3010 Supervision

(g) Definitions

(2) (A) A “branch office” is any location where one or more associated persons of a member regularly conducts the business of effecting any transactions in, or inducing or attempting to induce the purchase or sale of any security, or is held out as such, excluding:

(i) Any location that is established solely for customer service and/or back office type functions where no sales activities are conducted and that is not held out to the public as a branch office;

(ii) Any location that is the associated person’s primary residence; provided that:

a. Only one associated person, or multiple associated persons, who reside at that location and are members of the same immediate family, conduct business at the location;

b. The location is not held out to the public as an office and the associated person does not meet with customers at the location;

c. Neither customer funds nor securities are handled at that location;

d. The associated person is assigned to a designated branch office, and such designated branch office is reflected on all business cards, stationery, advertisements and other communications to the public by such associated person;

e. The associated person’s correspondence and communications with the public are subject to the member’s supervision in accordance with Rule 3010;

f. Electronic communications (e.g., e-mail) are made through the member’s electronic system;

g. All orders are entered through the designated branch office or an electronic system established by the member that is reviewable at the branch office;

h. Written supervisory procedures pertaining to supervision of sales activities conducted at the residence are maintained by the member; and

i. A list of the residence locations is maintained by the member;

(iii) Any location, other than a primary residence, that is used for securities business for less than 30 business days in any one calendar year, provided the member complies with the provisions of paragraph (A)(2)(ii)a. through h. above;

(iv) Any office of convenience, where associated persons occasionally and exclusively by appointment meet with customers, which is not held out to the public as an office;*

(v) Any location that is used primarily to engage in non-securities activities and from which the associated person(s) effects no more than 25 securities transactions in any one calendar year; provided that any advertisement or sales literature identifying such location also sets forth the address and telephone number of the location from which the associated person(s) conducting business at the non-branch locations are directly supervised;

(vi) The Floor of a registered national securities exchange where a member conducts a direct access business with public customers; or

(vii) A temporary location established in response to the implementation of a business continuity plan.

(B) Notwithstanding the exclusions provided in paragraph (2)(A), any location that is responsible for supervising the activities of persons associated with the member at one or more non-branch locations of the member is considered to be a branch office.

(C) The term "business day" as used in Rule 3010(g)(2)(A) shall not include any partial business day provided that the associated person spends at least four hours on such business day at his or her designated branch office during the hours that such office is normally open for business.

* Where such office of convenience is located on bank premises, signage necessary to comply with applicable federal and state laws, rules and regulations and applicable rules and regulations of the NYSE, other self-regulatory organizations, and securities and banking regulators may be displayed and shall not be deemed "holding out" for purposes of this section.

* * * * *

IM-3010-1. Standards for Reasonable Review

In fulfilling its obligations pursuant to Rule 3010(c), each member must conduct a review, at least annually, of the businesses in which it engages, which review must be reasonably designed to assist in detecting and preventing violations of and achieving compliance with applicable securities laws and regulations and with NASD rules. Each member shall establish and maintain supervisory procedures that must take into consideration, among other things, the member's size, organizational structure, scope of business activities, number and location of offices, the nature and complexity of products and services offered, the volume of business done, the number of associated persons assigned to a location, whether a location has a principal on-site, whether the office is a non-branch location, the disciplinary history of registered representatives or associated persons, etc. The procedures established and the reviews conducted must provide that the quality of supervision at remote offices is sufficient to assure compliance with applicable securities laws and regulations and with NASD rules. With respect to a non-branch location where a registered representative engages in securities activities, a member must be especially diligent in establishing procedures and conducting reasonable reviews. Based on the factors outlined above, members may need to impose reasonably designed supervisory procedures for certain locations and/or may need to provide for more frequent reviews of certain locations.

* * * * *

ATTACHMENT B—NYSE RULE

Rule 342. OFFICES - APPROVAL, SUPERVISION AND CONTROL

Supplementary Material:

.10 Definition of Branch Office

A “branch office” is any location where one or more associated persons of a member or member organization regularly conduct the business of effecting any transactions in, or inducing or attempting to induce the purchase or sale of any security, or is held out as such, excluding:

(A) any location that is established solely for customer service and/or back office type functions where no sales activities are conducted and that is not held out to the public as a branch office;

(B) any location that is the associated person’s primary residence; provided that: (i) only one associated person, or multiple associated persons, who reside at that location and are members of the same immediate family, conduct business at the location; (ii) the location is not held out to the public as an office and the associated person does not meet with customers at the location; (iii) neither customer funds nor securities are handled at that location; (iv) the associated person is assigned to a designated branch office, and such branch office is reflected on all business cards, stationery, advertisements and other communications to the public by such associated person; (v) the associated person’s correspondence and communications with the public are subject to all supervisory provisions of the Exchange’s rules including, but not limited to, Rules 342 and 472; (vi) electronic communications (e.g., e-mail) are made through the member’s or member organization’s electronic system; (vii) all orders are entered through the designated branch office or an electronic system established by the member or member organization that is reviewable at the branch office; (viii) written supervisory procedures pertaining to supervision of sales activities conducted at the residence are maintained by the member or member organization; and (ix) a list of the locations is maintained by the member or member organization;

(C) any location, other than a primary residence, that is used for securities business for less than 30 business days in any one calendar year, provided the member or member organization complies with the provisions of (ii) through (viii) of paragraph (B) above;

(D) any office of convenience, where the associated person occasionally and exclusively by appointment meets with customers, which is not held out to the public as a branch office (where such location is on bank premises, however, only signage required by the Interagency Statement (Statement on Retail Sales of Nondeposit Investment Products required under Banking Regulations) may be displayed);

(E) any location that is used primarily to engage in non-securities activities and from which the associated person effects no more than 25 securities transactions in any one calendar year; provided that any advertisements or sales literature identifying such location also sets forth the address and telephone number of the location from which the associated person conducting business at the non-branch locations are directly supervised;

(F) the Floor of a registered national securities exchange where a member or member organization conducts a direct access business with public customers; or

(G) a temporary location established in response to the implementation of a business continuity plan.

Notwithstanding the exclusions in subparagraphs 342.10(A) - (G), any location that is responsible for supervising the activities of persons associated with a member or member organization at one or more non-branch locations of such member or member organization is considered to be a branch office.

For purposes of this Rule, the term "business day" shall not include any partial business day provided that the associated person spends at least four hours on such business day at his or her designated branch office during the hours that such office is normally open for business.

For purposes of this Rule, the term "associated person of a member or member organization" is defined as a member, allied member, or employee associated with a member or member organization.

For purposes of Rule 342.10(B)(viii), written supervisory procedures shall include criteria for on-site for cause reviews of an associated person's primary residence. Such reviews must utilize risk-based sampling or other techniques designed to assure compliance with applicable securities laws and regulations and with NYSE rules.

For purposes of Rule 342.10(B)(viii) and (C), written supervisory procedures for such residences and other remote locations must be designed to assure compliance with applicable securities laws and regulations and with NYSE Rules.

Factors which should be considered when developing risk-based sampling techniques to determine the appropriateness of on-site for cause reviews of selected residences and other remote locations shall include, but not be limited to, the following: (i) the firm's size; (ii) the firm's organizational structure; (iii) the scope of business activities; (iv) the number and location of offices; (v) the number of associated persons assigned to a location; (vi) the nature and complexity of products and services offered; (vii) the volume of business done; (viii) whether the location has a Series 9/10-qualified person on-site; (ix) the disciplinary history of the registered persons or associated persons, including a review of such person's customer complaints and Forms U4 and U5; and (x) the nature and extent of a registered person's or associated person's outside business activities, whether or not related to the securities business.

* * *

Notice to Members

MARCH 2006

SUGGESTED ROUTING

Legal & Compliance
Operations
Senior Management

KEY TOPICS

Blue Sheets

ACTION REQUESTED

Intermarket Surveillance Group¹

Validation of Electronic Blue Sheet Systems:
**Intermarket Surveillance Group Requires Validation
by March 31, 2006**

Executive Summary

This *Notice to Members* reminds member firms that by March 31, 2006, they must complete validation of certain data fields that firms submit to the Electronic Blue Sheet (EBS) System, as directed in *Notice to Members 05-58*. If firms find any inconsistencies with overall EBS standards, this Notice advises them of deadlines for remediation of these inconsistencies.

This Notice was prepared by the following self-regulatory organizations (SROs) acting jointly as members of the Intermarket Surveillance Group (ISG):

- ▶ American Stock Exchange LLC (Amex)
- ▶ Boston Stock Exchange, Inc. (BSE)
- ▶ Chicago Board Options Exchange, Inc. (CBOE)
- ▶ Chicago Stock Exchange, Inc. (CHX)
- ▶ International Securities Exchange (ISE)
- ▶ NASD Inc. (NASD)
- ▶ National Stock Exchange (NSX)
- ▶ New York Stock Exchange, LLC (NYSE)
- ▶ Pacific Exchange, Inc. (PCX)
- ▶ Philadelphia Stock Exchange, Inc. (PHLX)

Questions/Further Information

Questions concerning this *Notice* may be directed to any of the following SRO staff:

SRO	Individual	Telephone No.	E-Mail
AMEX	Robert Ulmer	(212) 306-1283	<i>robert.ulmer@nasd.com</i>
BOX	Bruce Goodhue	(617) 235-2022	<i>bruce.goodhue@bostonstock.com</i>
CBOE	Pat Sizemore	(312) 786-7752	<i>sizemore@cboe.com</i>
CHX	Marguerite Donovan	(312) 663-2548	<i>mdonovan@chx.com</i>
NSX	Nicole Guiffra	(312) 786-8809	<i>guiffra@nsx.com</i>
ISE	Willie Wong	(212) 897-8126	<i>wwong@iseoptions.com</i>
NASD	Rose Braisted	(240) 386-4987	<i>rose.braisted@nasd.com</i>
NYSE	John Kroog	(212) 656-6532	<i>jkroog@nyse.com</i>
PCX	John Chapin	(312) 442-7790	<i>jchapin@pacificex.com</i>
PHLX	Christopher Swisher	(215) 496-5680	<i>chris.swisher@phlx.com</i>

If you have questions concerning the interpretation of SEC Rule 17a-25 under Section 17 of the Securities Exchange Act of 1934, or if you need to report problems concerning EBS submissions to the SEC, please contact:

Individual	Telephone No.	E-Mail
Joseph Cella	(202) 551-4951	<i>cellaj@sec.gov</i>
Alton Harvey	(202) 551-5691	<i>harveya@sec.gov</i>

ISG Regulatory Memorandum, ISG 2006-01

On September 7, 2005, SROs, acting jointly as members of the Intermarket Surveillance Group, issued ISG Regulatory Memorandum 2005-01 (the ISG Notice) concerning the automated submission of trading information via the Electronic Blue Sheet System.² The ISG Notice reiterated requirements for accurate and timely EBS reporting. The ISG Notice also required that by no later than March 31, 2006, members and member organizations conduct and complete a validation of all required EBS data to ensure that EBS transmissions are consistent with current standards and accurately reflect members' books and records. Attachment A of the ISG Notice, *Record Layout for Submission of Trading Information*, specified those layout records that required validation.

On February 6, 2006, the Securities Industry Association (SIA), on behalf of its member firms, requested that the ISG extend the validation due date. The SROs and representatives of the SIA have been engaged in discussions with respect to the EBS requirements, the time needed to complete the validation process, and the time needed to remediate the fields not meeting the requirements. Based on these discussions, there is no need to extend the validation date beyond the March 31, 2006 deadline, and, therefore, no extension will be granted. As stated in the ISG Notice, members and member organizations are required to retain documentation confirming that the validation has occurred.

Members and member organizations that have reported inconsistencies as outlined in the ISG Notice will have until July 31, 2006 to complete remediation. Any member or member organization that believes it has a compelling and appropriate reason for further delay must provide its designated SRO with a detailed written explanation and request by April 17, 2006. These requests will be evaluated on a case-by-case basis in discussions with that SRO. Extensions will be granted in only the most extreme cases. All members and member organizations that are correcting inconsistencies shall provide written confirmation to their designated SRO that remediation has been completed on or before July 31, 2006.

Members and member organizations are reminded that, except as modified by this memorandum, the guidance of the ISG Notice remains in full force and effect.

Endnotes

- 1 This ISG Notice 2006-01 was prepared by the following self-regulatory organizations as members of the ISG: American Stock Exchange LLC (AMEX), Boston Stock Exchange, Inc. (BSE), Chicago Board Options Exchange, Inc. (CBOE), Chicago Stock Exchange, Inc. (CHX), International Securities Exchange (ISE), NASD Inc. (NASD), National Stock Exchange (NSX), New York Stock Exchange, Inc. (NYSE), Pacific Exchange, Inc. (PCX) and Philadelphia Stock Exchange, Inc. (PHLX).
- 2 The ISG Notice 2005-01 was published for NASD members in *Notice to Members 05-58*.

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Disciplinary and Other NASD Actions

REPORTED FOR MARCH

NASD® has taken disciplinary actions against the following firms and individuals for violations of NASD rules; federal securities laws, rules and regulations; and the rules of the Municipal Securities Rulemaking Board (MSRB). The information relating to matters contained in this *Notice* is current as of the end of February 2006.

Firm Fined, Individual Sanctioned

First Securities USA, Inc. (CRD #39986, Irvine, California) and Stanley Clifton Brooks (CRD #31684, Registered Principal, San Clemente, California) submitted a Letter of Acceptance, Waiver and Consent in which they were fined \$60,000, jointly and severally, and the firm was censured, while Brooks was suspended from association with any NASD member in any supervisory capacity for two years. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Brooks, violated the supervision rule by failing to commence and complete compliance inspections that were undertakings in the firm's membership agreement.

Brooks' suspension began on March 6, 2006, and will conclude at the close of business on March 5, 2008. (NASD Case #E0220030046-02)

Firms and Individuals Fined

Balfour Investors, Inc. (CRD #7382, New York, New York), Harry Isaac Freund (CRD #214182, Registered Principal, New York, New York) and Jay Sheldon Goldsmith (CRD #224459, Registered Principal, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which they were censured and fined \$10,000, jointly and severally. Without admitting or denying the allegations, the respondents consented to the described sanctions and to the entry of findings that the firm, acting through Freund and Goldsmith, conducted a securities business while failing to maintain the required minimum net capital. (NASD Case #E1020041022-01)

Certes Capital Securities, LLC (CRD #124392, Deerfield, Illinois), Dean Richard Hedeker (CRD #2068563, Registered Principal, Buffalo Grove, Illinois), and James Patrick Kozak (CRD #2237880, Registered Principal, Glenview, Illinois) submitted an Offer of Settlement in which they were censured and fined \$40,000, 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 Hedeker and Kozak, violated the

registration provisions by permitting an individual to act in a capacity requiring registration when he was not registered. The findings stated that the firm, acting through Hedecker and Kozak, allowed the individual to exert control and/or direct certain of its operations, including participating in employment-related decisions and coordinating the firm's private placement offerings. The findings also stated that the firm, acting through Hedecker and Kozak, failed to amend the firm's Form BD to disclose the individual's role there and failed to supervise the associated unregistered individual. The findings further stated that the respondents engaged in violations in connection with two private placements by not properly escrowing funds and prematurely releasing funds before the minimums were met. **(NASD Case #C8A050023)**

Firms Fined

Advanced Equities, Inc. (CRD #35545, Chicago, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$17,500. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to provide notification two business days prior to making capital withdrawals, when these withdrawals exceeded the aggregate amount as required by SEC Rule 15c3-1(e)(1). NASD also found that the firm failed to qualify and register an options principal, and failed to adequately and properly supervise the options activity conducted there. **(NASD Case #E8A2004000301)**

Coldstream Securities, Inc. (CRD #46835, Bellevue, Washington) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to adopt and implement an anti-money laundering (AML) program reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act (BSA) and the regulations promulgated thereunder. **(NASD Case #E3B2004000801)**

Direct Access Brokerage Services, Inc. (CRD #30057, Chicago, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$17,500. Without admitting or denying the

allegations, the firm consented to the described sanctions and to the entry of findings that it incorrectly reported the "second leg" of NASDAQ National Market (NNM) riskless principal transactions to the Automated Confirmation Transaction SystemSM (ACTSM) for which it was not the firm with the obligation to report the trade. NASD found that the firm executed short sale transactions and failed to report them to ACT with a short sale modifier. NASD also found that the firm executed transactions based on a prior reference point in time, and failed to report each of these transactions to ACT with a prior reference point modifier. 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 concerning trade reporting for trades executed on a prior reference point. **(NASD Case #E8A2004013003)**

E*Trade Professional Trading, LLC (CRD #39293, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured 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 reports with respect to equity securities traded on the Nasdaq Stock Market to the Order Audit Trail SystemSM (OATSSM) that were not in the NASD-prescribed electronic form, and the firm failed to repair them. The findings stated that the firm also failed to enforce its written supervisory procedures governing the repair and replacement of rejected OATS reports, and thereby failed to provide supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and NASD rules concerning OATS data transmission. **(NASD Case #20042000034-01)**

Ferris, Baker Watts Incorporated (CRD #285, Washington, District of Columbia) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$15,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that in transactions for or with a customer, it failed to use reasonable diligence to ascertain the best inter-dealer market, and failed to buy or sell in such market so that its customer's resultant price was as favorable as possible under prevailing market conditions. The findings stated that the firm failed to report the

correct price of the transaction in last sale reports of transactions in eligible securities through NASDAQ. The findings also included that the firm, when it acted as principal for its own account, failed to provide written notification disclosing the correct reported trade price to its customer. (NASD Case #20042000122-01)

Fimat USA, LLC (CRD #36118, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to timely report Reportable Order Events (ROEs) to OATS. NASD found that the firm failed to enforce its written supervisory procedures that specified that the designated principal must conduct a daily review of the OATS Web site to ensure that all OATS files are accepted and to identify any late OATS reports. (NASD Case #20050006366-01)

First Hudson Financial Group, Inc., (CRD #32926, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$15,000, required to pay \$7,792.75, plus interest, in restitution to public customers, and required to retain an independent consultant to review and make written recommendations for the firm's implementation of a supervisory system and procedures reasonably designed to ensure that charged commissions are fair, reasonable, not excessive and adequately disclosed to customers. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that, while acting through a registered representative, it charged unreasonable and excessive option commissions on eight covered calls ranging from 5.3 percent to 54 percent. NASD found that the firm routinely charged its public customers commissions of less than 5 percent for equity securities and covering options purchases to close pre-existing option positions. In contrast, the firm, in certain instances, charged customers greater commissions, as high as 54 percent, for the sale of covered calls, particularly where the transactions were not part of a simultaneous buy-write strategy. The findings stated that the firm erred in treating the equity and options transactions as one transaction for the purposes of calculating and assessing the charged commission's appropriateness, particularly where the transactions were not part of a simultaneous buy-write strategy.

The findings also stated that the firm failed to have an adequate supervisory system in place to prevent and detect excessive commissions in options transactions. (NASD Case #E1020040299-01)

First Montauk Securities Corp. (CRD #13755, Red Bank, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$50,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to implement and enforce a written AML program that was reasonably designed to achieve compliance with the requirements imposed by the BSA and the regulations promulgated thereunder. NASD found that the firm's equity transaction confirmations failed to indicate that it was a market maker in the security, and that the number of shares was inaccurate on another transaction. NASD also found that the order tickets the firm completed revealed deficiencies, in that they failed to identify the terms and conditions of the order, did not contain time stamps, contained an illegible time stamp, contained an execution time stamp that was subsequent to the trade report time, did not contain the customer account number or an execution price. The findings stated that the firm reported transactions in municipal securities to the MSRB that did not contain the correct trade time or correct price. The findings also stated that the firm reported to the Trade Reporting and Compliance Engine (TRACE) TRACE-eligible securities transactions with the following deficiencies: incorrect prices, late reporting, incorrect execution times, incorrectly reported as customer trades, reported with an incorrect volume, reported when in fact no such trade had taken place, and failed to report a cancelled transaction. In addition, the findings stated that the firm's supervisory system and written procedures were not reasonably designed to achieve compliance with respect to the applicable securities laws and regulations concerning TRACE reporting. (NASD Case #E9B2005005003)

Freedom Investments, Inc. (CRD #37674, Edison, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$20,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to conduct an independent test of its AML program, and failed to have written procedures to address the firm's obligation to

provide prompt notification to NASD regarding changes to their AML contact information. NASD also found that the firm failed to enforce its Suspicious Activity Reports (SARs) procedures, in that the firm rejected at least seven questionable transactions involving ACH deposit requests which were classified as “fraudulent” on its internal books and records. The firm subsequently restricted and closed the accounts but never filed SARs for these transactions. The findings also stated that the firm improperly extended credit in violation of Reg. T, by failing to promptly cancel or liquidate the transactions in cash accounts where customers had used ACH deposits to pay for securities transactions, but their deposits failed to clear. **(NASD Case #E9B2004004401)**

GFI Securities, LLC (CRD #19982, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$25,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed, within 90 seconds after execution, to transmit last sale reports of transactions in Consolidated Quotation Services (CQS) through NASDAQ, and failed to designate some last sale reports as late. **(NASD Case #20050000636-01)**

J.P. Morgan Securities Inc. (CRD #18718, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$115,000 and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations, and NASD rules concerning ACT reporting and trade reporting. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it transmitted last sale reports of transactions in NNM securities through ACT and failed to designate them as reflecting a price different from the current market when the execution was based on a prior reference point in time. The findings stated that the firm failed to report the correct symbol indicating whether the transaction was a “buy,” “sell” or “cross” in last sale reports of transactions in eligible securities through ACT. NASD found that the firm failed, within 90 seconds after execution, to transmit last sale reports of transactions in eligible securities through ACT, and failed to designate them as late. The findings also stated that the firm failed to report the correct symbol indicating whether it executed transactions in eligible securities in a principal or agency capacity to ACT. In addition, the

findings stated that the firm reported last sale reports of transactions in NNM securities, eligible securities through ACT and in OTC Equity securities that it was not required to report. NASD also found that the firm’s supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and NASD rules concerning ACT reporting and trade reporting. **(NASD Case #20042000159-01)**

Lehman Brothers Inc. (CRD #7506, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$95,000, ordered to pay \$5,933.04, plus interest, in restitution to public customers and required to revise the firm’s written supervisory procedures regarding compliance with NASD Conduct Rule 2320. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that in customer transactions, the firm failed to use reasonable diligence to ascertain the best inter-dealer market, and failed to buy or sell in such market so that its customers’ resultant prices were as favorable as possible under prevailing market conditions. The findings also stated that the firm double-reported a riskless principal execution, failed to report riskless principal trades correctly and failed to disclose the correct capacity on customer confirmations. The findings also included that the firm’s supervisory system failed to provide for supervision reasonably designed to achieve compliance with NASD Conduct Rule 2320 with respect to its obligation to use reasonable diligence to ascertain the best inter-dealer market, and to buy or sell in such market so that its customers’ resultant price was as favorable as possible under prevailing market conditions. **(NASD Case #20042000082-01)**

Merrill Lynch, Pierce, Fenner & Smith, Inc. (CRD #7691, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$20,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to reasonably and promptly respond to “red flags” raised by customer complaints, written communications and telephone conversations regarding possible use of discretion by a registered representative and failed to institute heightened supervisory procedures targeting possible use of discretion by the representative. **(NASD Case #E062002029302)**

Nationwide Securities, Inc. (CRD #11173, Newark, Delaware) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$30,750. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it filed Uniform Termination Notices for Securities Industry Registration (Form U5) late, and failed to timely amend Uniform Applications for Securities Industry Registration or Transfer (Forms U4) and Forms U5. The findings also stated that the firm failed to prepare adequate written supervisory procedures associated with Forms U4 and U5 filing requirements. NASD also found that the firm failed to timely file 3070 reports. (NASD Case #E8A200540145)

Neuberger Berman, LLC (CRD #2908, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$15,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that, for inclusion on the Consolidated Tape, it reported a last sale report of a transaction in an eligible security that resulted from a private offering after normal market hours that the firm was not required to report. The findings stated that the firm failed to report through NASDAQ the correct symbol indicating whether the transaction was a "buy," "sell" or "cross." The findings also stated that the firm failed to report the correct symbol indicating whether it executed the transaction in a principal or agency capacity. (NASD Case #20050000876-01)

Newbridge Securities Corporation (CRD #104065, Ft. Lauderdale, Florida) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$35,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to immediately display customer limit orders in NASDAQ securities in its public quotation, when each such order was at a price that would have improved the firm's bid or offer in each such security; or when the order was priced equal to the firm's bid or offer and the national best bid or offer for each such security, and the size of the order represented more than a *de minimis* change in relation to the size associated with the firm's bid or offer in each such security. The findings also stated that the firm transmitted reports to OATS that contained inaccurate, incomplete or improperly

formatted data in that the reports omitted the "Not Held" indicator, omitted the order route reports, or failed to match a NASDAQ trade report. NASD also found that the firm failed, within 90 seconds after execution, to transmit last sale reports of transactions in OTC Equity securities through NASDAQ, and failed to designate some as late. The findings also included that the firm executed riskless principal transactions in OTC Equity securities and reported to NASDAQ that it executed the transactions in a principal only capacity, without submitting separate clearing only, or non-tape, non-clearing reports with capacity indicators of "riskless principal." (NASD Case #20042000065-01)

Oppenheimer & Co. Inc. (CRD #249, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$20,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to file an MSRB Form G-36 and an official statement for three underwritings to the MSRB in a timely manner. The findings also stated that the firm filed inaccurate MSRB Forms G-37 and failed to submit information in writing on consulting arrangements to issuers with which it was seeking municipal securities business. (NASD Case #E102003017701)

Smith, Moore & Co. (CRD #3441, Clayton, Missouri) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$20,000 and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations concerning short-interest reporting. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to report its short-interest positions in various securities to NASD. The findings stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations concerning short-interest reporting. (NASD Case #20042000040-01)

Spencer Edwards, Inc. (CRD #22067, Englewood, Colorado) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and required to revise its written supervisory procedures with respect to applicable securities laws and regulations, and NASD rules concerning trade reporting.

In light of the firm's financial status, NASD imposed a \$10,000 fine. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed, within 90 seconds after execution, to transmit last sale reports of transactions in OTC Equity securities through ACT, and failed to designate them as late. The findings stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and NASD rules concerning trade reporting. NASD found that the firm failed, within 90 seconds after execution, to transmit last sale reports of transactions in OTC Equity securities to NASDAQ, and failed to designate them as late. **(NASD Case #20042000139-01)**

State Farm VP Management Corp. (CRD #43036, Bloomington, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$133,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to timely file a Form U5 for individuals whose registrations were terminated. NASD found that the firm failed to establish and maintain a supervisory system that was reasonably designed to achieve compliance with respect to applicable securities laws and regulations, and NASD rules to ensure the timely filing of Forms U5. **(NASD Case #E8A2005019201)**

Westcap Securities, Inc. (CRD #45250, Irvine, California) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to develop and implement a written AML program reasonably designed to achieve and monitor compliance with the requirements of the BSA and the regulations promulgated thereunder, in that the firm's program failed to have procedures to (1) perform customer identification, (2) independently test the AML compliance program and (3) document ongoing training. NASD also found that Westcap failed to implement procedures to adequately monitor and detect suspicious activity. **(NASD Case #E0220050170-02)**

Westminster Securities Corporation (CRD #6105, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$10,000 and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations, and NASD rules concerning maintaining two-sided quotations. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to maintain continuous two-sided quotations with respect to securities in the absence of the grant of an excused withdrawal or a functional excused withdrawal by NASD. The findings stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and NASD rules concerning maintaining two-sided quotations. **(NASD Case #20042000131-01)**

Wharton Equity Corporation (CRD #10170, Wayne, Pennsylvania) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that its written AML program was not reasonably designed to achieve compliance with the BSA and the regulations promulgated thereunder. **(NASD Case #E9A2005013302)**

Wolfe & Hurst Bond Brokers Inc. (CRD #8288, Jersey City, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$15,000 and required to revise its written supervisory procedures with respect to the applicable securities laws and regulations, and NASD rules concerning TRACE. Without admitting or denying the allegations, the firm consented to the described sanctions and to the entry of findings that it failed to report transactions in TRACE-eligible securities executed on a business day during TRACE system hours to TRACE within 45 minutes of the execution time. The findings stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with respect to the applicable securities laws and regulations, and NASD rules concerning TRACE reporting. **(NASD Case #20050001505-01)**

Individuals Barred or Suspended

Marco Alfonsi (CRD #2770342, Registered Principal, Hicksville, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$25,000 and suspended from association with any NASD member in all principal capacities for one year. Without admitting or denying the allegations, Alfonsi consented to the described sanctions and to the entry of findings that he failed to establish and maintain a supervisory system and written supervisory procedures for his member firm that were reasonably designed to achieve compliance with the applicable securities laws, regulations and NASD rules. Specifically, Alfonsi failed to establish a system to ensure that the firm maintained correspondence and internal communications, complete customer complaint files and customer new account information. Also, NASD found that Alfonsi failed to ensure that the firm filed customer complaints in a timely manner under NASD Rule 3070 and to ensure that Forms U5 were timely amended.

Alfonsi's suspension began on February 21, 2006, and will conclude at the close of business on February 20, 2007. (NASD Case #E072004010401)

Patrick Alexander Anthony (CRD #2080102, Registered Principal, Los Angeles, California) submitted an Offer of Settlement in which he was fined \$10,000, suspended from association with any NASD member in any capacity for two years, barred from association with any NASD member in any principal capacity and required to pay \$77,400, plus interest, in restitution to public customers. Satisfactory proof of restitution payment must be made before Anthony reassociates with any NASD member. Without admitting or denying the allegations, Anthony consented to the described sanctions and to the entry of findings that he, directly or indirectly, by the use of means or instrumentalities of interstate commerce or the mails, employed artifices, devices, or schemes to defraud, made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; engaged in acts, practices, or courses of business that operated or would operate as a fraud or deceit; and/or effected transactions in, or induced the purchase or sale of, securities by means of manipulative, deceptive, or other fraudulent devices or contrivances by making material

misrepresentations and omissions in offers and sales of debt securities of an issuer, for which he was the sole officer, director and shareholder.

Anthony's suspension began on February 6, 2006, and will conclude at the close of business on February 5, 2008. (NASD Case #E0720031136-02)

Bradley Allan Bervert (CRD #2563245, Registered Principal, Overland Park, Kansas) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Bervert consented to the described sanction and to the entry of findings that he failed to appear for an NASD on-the-record interview. (NASD Case #E0420040290-01)

Prashant Biraj Bhuyan (CRD #4201934, Registered Representative, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was censured, fined \$5,000 and suspended from association with any NASD member in any capacity for six months. In light of Bhuyan's financial status, the imposed fine is \$5,000, and it must be paid before Bhuyan reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Bhuyan consented to the described sanctions and to the entry of findings that he executed short sale transactions in a security listed on a national securities exchange at or below the current inside bid when the current inside bid was below the preceding inside bid on the security. The findings also stated that Bhuyan executed short sale orders and failed to properly mark the order tickets for those orders as short. The findings also included that Bhuyan executed short sale orders in a security and, for each order, failed to make an affirmative determination that he would receive delivery of the security on the customer's behalf or that he could borrow the security on the customer's behalf for delivery by the settlement date.

Bhuyan's suspension began on March 6, 2006, and will conclude at the close of business on September 5, 2006. (NASD Case #20050000026-01)

Matthew Gregory Blackburn (CRD #4627265, Registered Representative, Westlake, Ohio) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity

for 60 days. The fine must be paid before Blackburn reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Blackburn consented to the described sanctions and to the entry of findings that he affixed a public customer's signature on an IRA 1035 transfer form without the customer's knowledge and consent, and sent the form to his member firm's home office for processing.

Blackburn's suspension began on March 6, 2006, and will conclude at the close of business on May 4, 2006. (NASD Case #2005000387601)

Gerald Arthur Brookshire (CRD #4709592, Registered Principal, Eagle, Idaho) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Brookshire consented to the described sanction and to the entry of findings that he prepared and submitted forged life insurance policy applications to an insurance company on a customer's behalf without the customer's knowledge, consent or authorization. (NASD Case #E3B20040210-01)

Saverio Cataldo (CRD #2746819, Registered Representative, Seaford, New York) submitted an Offer of Settlement in which he was suspended from association with any NASD member in any capacity for nine months. In light of Cataldo's financial status, the sanctions do not include a monetary fine, restitution or disgorgement. Without admitting or denying the allegations, Cataldo consented to the described sanction and to the entry of findings that he directly or indirectly, by the use of means or instrumentalities of interstate commerce or the mails, employed artifices, devices, or schemes to defraud; made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; engaged in acts, practices, or courses of business that operated or would operate as a fraud or deceit; and/or effected transactions in, or induced the purchase or sale of, securities by means of manipulative, deceptive, or other fraudulent devices or contrivances by excessively trading the customer's account. The findings also stated that Cataldo recommended and effected securities transactions in the account of a public

customer that were unsuitable for the customer in view of the size and frequency of the transactions, the nature of the account and the customer's financial situation, investment objectives and needs. NASD also found that Cataldo's suitability violations include use of margins that was inappropriate for the customer.

Cataldo's suspension began on February 21, 2006, and will conclude at the close of business on November 20, 2006. (NASD Case #E9B2003032501)

James Willard Clark (CRD #1225726, Registered Principal, Frisco, Texas) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any principal or supervisory capacity for 30 days. Without admitting or denying the allegations, Clark consented to the described sanctions and to the entry of findings that he failed to supervise a registered representative's offers and sales of securities that were unsuitable for the customer because they were, among other things, inconsistent with the customer's objectives. NASD also found that Clark failed to supervise the registered representative's unsuitable sale of a variable annuity to a public customer.

Clark's suspension began on February 6, 2006, and concluded at the close of business on March 7, 2006. (NASD Case #E062003043402)

Frank Collins (CRD #1942411, Registered Principal, Seaford, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Collins consented to the described sanction and to the entry of findings that he did not promptly perform his supervisory responsibilities, altered the dates of the firm's mutual fund exception reports and added inaccurate information to surveillance reports. The findings stated that Collins failed to disclose the alterations to the exception reports to his member firm and as a result, caused the firm to provide NASD with inaccurate information. (NASD Case #E0220030854-02)

Colin Price Collea (CRD #1519299, Registered Representative, Littleton, Colorado) was fined \$25,000 and suspended from association with any NASD member in any capacity for two years. The fine must be paid before Collea reassociates with any NASD

member following the suspension, or before he requests relief from any statutory disqualification. The sanctions were based on findings that Collea made material misrepresentations to public customers in connection with Callable Certificate of Deposit offers and sales.

Collea's suspension began on February 2, 2006, and will conclude on February 2, 2008. **(NASD Case #C05050026)**

John Kent Colvin (CRD #2811349, Registered Representative, Nashville, Tennessee) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Colvin consented to the described sanction and to the entry of findings that he engaged in private securities transactions for compensation without providing written notification to, or obtaining prior approval from, his member firm. **(NASD Case #C05050030)**

Melvin Conway (CRD #1257697, Registered Representative, Monroe, Louisiana) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for three months. The fine must be paid before Conway reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Conway consented to the described sanctions and to the entry of findings that he directed an unassociated person to forge a public customer's signature on forms necessary to effect the customer's authorized purchase.

Conway's suspension began on February 21, 2006, and will conclude on May 20, 2006. **(NASD Case #E052004032401)**

Richard Patrick Corl (CRD #3143352, Registered Principal, Bryn Mawr, Pennsylvania) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Corl consented to the described sanction and to the entry of findings that he obtained a \$15,090 check payable to an affiliate company of his member firm, endorsed the check, deposited the funds into his personal account and converted them for his personal use and benefit without authorization. **(NASD Case #2005003236401)**

James Daniel David (CRD #1644953, Registered Representative, Spokane, Washington) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for three months. The fine must be paid before David reassociates with any NASD member following the suspension, or before he request relief from any statutory disqualification. Without admitting or denying the allegations, David consented to the described sanctions and to the entry of findings that he willfully misrepresented a material fact on a Form U4.

David's suspension began on February 21, 2006, and will conclude on May 20, 2006. **(NASD Case #E3B2004023201)**

Jatinder Dua (CRD #4523365, Registered Representative, Cockeysville, Maryland) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Dua consented to the described sanction and to the entry of findings that he forged a supervisor's signature on a letter containing an apology for providing false information, and sent it to a public customer without the supervisor's knowledge or authorization. The findings also stated that Dua failed to respond to NASD requests for information. **(NASD Case #2005002107001)**

Justin F. Ficken (CRD #4059611, Registered Representative, Boston, Massachusetts) was barred from association with any NASD member in any capacity. The National Adjudicatory Council (NAC) imposed the sanction following an appeal of an Office of Hearing Officers (OHO) decision. The sanction was based on findings that Ficken failed to appear for an NASD on-the-record interview.

This action has been appealed to the Securities and Exchange Commission (SEC), and all sanctions, other than the bar, are not in effect pending consideration of the appeal. **(NASD Case #C11040006)**

Charles Edward Fleming (CRD #1447158, Registered Principal, Colleyville, Texas) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Fleming consented

to the described sanctions and to the entry of findings that, in order to effect a securities transaction for compensation, he signed public customers' names on an "Authorization to Transfer Fund" form.

Fleming's suspension began on February 6, 2006, and concluded at the close of business on March 7, 2006. (NASD Case #2005001076502)

Michael James France (CRD #3176408, Registered Representative, Cherry Hill, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for 10 business days. The fine must be paid before France reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, France consented to the described sanctions and to the entry of findings that he signed a Life Insurance Company Fixed Annuity Application as having witnessed a public customer signing the application when in fact, he did not witness it.

France's suspension began on March 6, 2006, and will conclude at the close of business on March 17, 2006. (NASD Case #2005000090701)

Louis Joseph Galeotafiore, Jr. (CRD #216688, Registered Principal, Flushing, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$7,500 and suspended from association with any NASD member for 10 business days as a Financial and Operations Principal (FINOP). Without admitting or denying the allegations, Galeotafiore consented to the described sanctions and to the entry of findings that the firm, acting acting through Galeotafiore, conducted a securities business when the firm's net capital fell below the minimum amount required by SEC Rule 15c3-1. NASD found that his former member firm, acting through Galeotafiore, failed to prepare and file accurate FOCUS Reports.

Galeotafiore's suspension began on March 6, 2006, and will conclude at the close of business on March 17, 2006. (NASD Case #ELI20030464-03)

Thomas Charles Garretson (CRD #3028617, Registered Representative, Alta Loma, California) submitted an Offer of Settlement in which he was fined \$5,000 and suspended from association with any

NASD member in any capacity for 60 days. The fine must be paid before Garretson reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Garretson consented to the described sanctions and to the entry of findings that, in connection with securities transactions in a public customer's account, he falsely indicated on the order memoranda that the transactions were unsolicited and placed a false date on a mutual fund switch form to indicate that the customer had signed it on or about the time of the subject transactions.

Garretson's suspension began on January 3, 2006, and concluded at the close of business on March 3, 2006. (NASD Case #C02050048/E0220030711-04)

Anthony J. Gaspero (ID #11021604, Unregistered Associated Person, Monee, Illinois) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegation, Gaspero consented to the described sanction and to the entry of findings that he engaged in securities business without being registered with NASD in any capacity. (NASD Case #C8A050023/E8A20030506)

Juliette Suzanne Gleason (CRD #1648485, Registered Principal, Duxbury, Massachusetts) submitted a Letter of Acceptance, Waiver and Consent in which she was fined \$15,000, which includes a \$5,000 fine and \$10,000 in disgorgement of commissions, and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Gleason reassociates with any NASD member following the suspension, or before she requests relief from any statutory disqualification. Without admitting or denying the allegations, Gleason consented to the described sanctions and to the entry of findings that she participated in private securities transactions for compensation without providing prior written notice to, and receiving prior written approval from, her member firm.

Gleason's suspension began on March 6, 2006, and will conclude at close of business on March 5, 2007. (NASD Case #E0220030722-01)

Diana Lynn Adkins Godwin (CRD #4138073, Registered Representative, Dagsboro, Delaware) submitted a Letter of Acceptance, Waiver and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Godwin consented to the described sanction and to the entry of findings that she made unauthorized withdrawals totaling \$19,550 from public customers' bank accounts and converted these funds for her own use and benefit. **(NASD Case #2005003229001)**

Eric Matthew Grace (CRD #2240979, Registered Principal, Redondo Beach, California) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Grace reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Grace consented to the described sanctions and to the entry of findings that he engaged in outside business activities without providing prompt written notice to his member firm. The findings also stated that Grace participated in private securities transactions and failed to provide prior written notice to, and receive prior written approval from, his member firm.

Grace's suspension began on March 6, 2006, and will conclude on March 5, 2007. **(NASD Case #E0220040695-01)**

Bruce Allan Hager (CRD #1358936, Registered Principal, Fargo, North Dakota) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Hager consented to the described sanction and to the entry of findings that he participated in outside business activities for compensation without providing prompt written notice to his member firm. The findings stated that Hager provided misleading information to NASD. **(NASD Case #E0420040447-01)**

Jason James Hachtel (CRD #4421009, Registered Representative, Cottage Grove, Wisconsin) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Hachtel consented to the described

sanction and to the entry of findings that he forged public customers' signatures on new and updated investment advisory agreements in order to change the agent of record on the investment advisory accounts without the customers' knowledge or consent. **(NASD Case #20050012181-01)**

Brett Aaron Jurica (CRD #2535339, Registered Principal, Scottsdale, Arizona) was barred from association with any NASD member in any capacity. The sanction was based on the findings that Jurica repeatedly misused a public customer's funds, in that he transferred funds and securities proceeds from the customer's accounts to an account he controlled for his own use and benefit without the customer's knowledge, authorization or consent. The findings stated that Jurica willfully failed to provide written notification to his member firm that he opened securities accounts at other broker-dealers, and failed to advise the other broker-dealers of his association with his member firm. The findings further stated that Jurica failed to respond to NASD requests for information. **(NASD Case #E3A2004031001)**

James Neal John (CRD #1593232, Registered Representative, Denton, Texas) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, John consented to the described sanction and to the entry of findings that he forged public customers' signatures on forms and submitted them to his member firm. **(NASD Case #2005002308401)**

Daniel Soohwan Kim (CRD #2598668, Registered Representative, Santa Ana, California) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Kim consented to the described sanction and to the entry of findings that he converted \$150,000 from public customers' variable life insurance policy accounts for his own personal use. **(NASD Case #E0220040441-01)**

Rena Logan (CRD #3000154, Registered Representative, Union, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which she was fined \$5,000 and suspended from association with any NASD member in any capacity for two months. Without admitting or denying the allegations, Logan

consented to the described sanctions and to the entry of findings that she settled a complaint with a public customer by paying the customer \$500 without her member firm's knowledge or approval.

Logan's suspension began on February 21, 2006, and will conclude at the close of business on April 20, 2006. (NASD Case 2005001788701)

Marc Alan Luxenberg (CRD #2091350, Registered Representative, Bellmore, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Luxenberg consented to the described sanction and to the entry of findings that he altered a registered representative's lapsed insurance license by changing the dates to falsely reflect proper state registration without the representative's knowledge, authorization or consent. (NASD Case #2005002187801)

Timothy Merrill Martin (CRD #2250279, Registered Representative, Dayton, Ohio) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Martin consented to the described sanction and to the entry of findings that he obtained \$50,000 from a public customer for his own use and benefit even though his member firm prohibited its representatives from borrowing or accepting funds from customers. The findings also stated that Martin deposited the \$50,000 into the customer's checking account, prepared a \$50,000 check drawn on the customer's account payable to Martin's wife, which the customer signed, deposited the check into a bank account in his wife's name, and used the funds in the account for his benefit—not the customer's. The findings also included that Martin made a written entry in the customer's check register falsely identifying the \$50,000 check as payable to a company and not his wife. NASD found that Martin prepared and provided the customer with a promissory note to repay the \$50,000, but failed to adhere to the note's terms. (NASD Case #E8A2004045402/C8A050023)

Peter Frederick McKinnon (CRD #1584788, Registered Principal, Beaverton, Oregon) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the

allegations, McKinnon consented to the described sanction and to the entry of findings that he converted \$180,000 from public customers' accounts for his own personal use. The findings stated that McKinnon failed to respond to NASD requests for documents and information. (NASD Case #E3B20040159-01)

Chris Lamont Meacham (CRD #1366969, Registered Principal, Poway, California) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 10 business days. The fine must be paid before Meacham reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Meacham consented to the described sanctions and to the entry of findings that he failed to promptly amend his Form U4 to disclose material information.

Meacham's suspension began on March 6, 2006, and will conclude at the close of business on March 17, 2006. (NASD Case #20050017095-01)

Carlos Omar Medina (CRD #4078775, Registered Representative, North Miami Beach, Florida) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Medina consented to the described sanction and to the entry of findings that, in connection with the sale of an unregistered security, he falsified documents and acted unethically by knowingly providing false information to his member firm to deceive and mislead the firm while it was investigating the facts and circumstances of the unregistered security sale. (NASD Case #E072004088501)

Daniel Micaletti, Jr. (CRD #2895242, Associated Person, Newport Beach, California) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for three months. The fine must be paid before Micaletti reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Micaletti consented to the described sanctions and to the entry of findings that he willfully failed to disclose material information on his Form U4.

Micaletti's suspension began on February 6, 2006, and concluded at the close of business on May 5, 2006. (NASD Case #2005001181101)

Raymond Jude Murphy (CRD #3278046, Registered Principal, Bloomfield, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$10,211.21, which included a disgorgement of \$211.21 in financial benefits received, suspended from association with any NASD member in any capacity for three months, and ordered to pay member firms \$1,526, plus interest, in restitution. The fine and restitution amounts must be paid before Murphy reassociates with a member firm following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Murphy consented to the described sanctions and to the entry of findings that he knowingly and intentionally entered one-share orders, through the NASDAQ National Market Execution System (NNMS) to market makers in NASDAQ securities, through his proprietary trading account at his member firm, at prices that he knew would receive an execution and improve, and were intended to improve each market maker's bid or offer in the subject security. The findings stated that Murphy knew that these market makers utilized proprietary trading systems that automatically updated their bids or offers to prices that were inferior to the National Best Bid and Offer (NBBO) if the market makers were quoting 100 shares with no reserve size and their quote was executed against a one-share order. The findings also included that immediately after receiving executions on the one-share orders in the subject securities which updated both the bid and offer, Murphy knowingly and intentionally entered larger orders on the other side of the market to buy and sell shares of securities in a firm proprietary trading account to receive a more favorably priced execution at the new inside bid or offer Murphy caused to be created. NASD found that Murphy was able to buy shares of securities at prices that were lower and sell shares of securities at prices that were higher than he would otherwise have been able to obtain.

Murphy's suspension began on March 6, 2006, and will conclude at the close of business on June 5, 2006. (NASD Case #20042000046-01)

Clyde Nakaoka (CRD #1033250, Registered Supervisor, Ontario, California) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for one year. The fine must be made before Nakaoka reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Nakaoka consented to the described sanctions and to the entry of findings that he willfully failed to amend his Form U4 to disclose a material fact.

Nakaoka's suspension began on January 3, 2006, and will conclude at the close of business on January 2, 2007. (NASD Case #2005002116901)

Cary Lancaster Olson (CRD #2435229, Registered Principal, Sparks, Nevada) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for one month. Without admitting or denying the allegations, Olson consented to the described sanctions and to the entry of findings that he exercised discretion in public customers' accounts without obtaining their written authorization to exercise discretion, and his member firm's written acceptance of the accounts as discretionary.

Olson's suspension began on March 6, 2006, and will conclude at the close of business on April 5, 2006. (NASD Case #E0120040219-01)

Russell Palermo (CRD #4392276, Registered Representative, Huntley, Illinois) submitted an Offer of Settlement in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Palermo consented to the described sanction and to the entry of findings that he received \$1,215 from public customers to purchase insurance, failed to apply the funds as directed by the customers, and, instead, used the funds to pay for his office expenses. The findings stated that Palermo failed to timely respond to NASD requests for information and documents. (NASD Case #2005000118401)

Nancy Lee Paquette (CRD #4320794, Registered Representative, Delafield, Wisconsin) submitted a Letter of Acceptance, Waiver and Consent in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Paquette consented to the described sanction and to the entry of findings that she engaged in a pattern of providing inaccurate, incomplete and misleading information to NASD, in correspondence and while under oath, that hindered an investigation and interfered with NASD's regulatory function. The findings stated that Paquette was being investigated for false life insurance policies she purportedly sold to a construction company's employees. **(NASD Case #E8A2004041101)**

Leonard Joseph Reiss (CRD #4335600, Registered Representative, Newton, Kansas) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 30 business days. The fine must be paid before Reiss reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Reiss consented to the described sanctions and to the entry of findings that he borrowed \$10,000 from public customers in contravention of his member firm's written procedures prohibiting representatives from borrowing money from customers.

Reiss' suspension began on February 21, 2006, and will conclude at the close of business on April 3, 2006. **(NASD Case #20050023200-01)**

Justin Eric Rhodes (CRD #4218246, Registered Representative, Reardan, Washington) submitted a Letter of Acceptance, Waiver and Consent in which he was suspended from association with any NASD member in any capacity for six months. In light of Rhodes' financial status, no monetary sanction has been imposed. Without admitting or denying the allegations, Rhodes consented to the described sanction and to the entry of findings that he engaged in a private securities transaction without prior written notice to, and approval from, his member firm.

Rhodes' suspension began on February 21, 2006, and will conclude on August 20, 2006. **(NASD Case #E3B2004016701)**

Aaron Talamayan Ronquillo (CRD #4952541, Associated Person, San Diego, California) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Ronquillo consented to the described sanction and to the entry of findings that he willfully failed to disclose material information on his Form U4. **(NASD Case #20050019363-01)**

Pierre Samuel Rosa (CRD #1106083, Registered Representative, Newport News, Virginia) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Rosa consented to the described sanction and to the entry of findings that he received \$13,200 from a public customer for investment purposes, but did not invest the funds as agreed. He instead converted the funds for his own use and benefit. NASD found that, prompted by his member firm's investigation in connection with the funds he had converted, Rosa prepared a fictitious letter addressed to himself that the customer purportedly had sent to him regarding the customer's investment, forged the customer's signature and provided a copy to his member firm as if it was genuine. **(NASD Case #2005001923301)**

David Michael Rosenberg (CRD #2165342, Registered Representative, Sarasota, Florida) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Rosenberg consented to the described sanction and to the entry of findings that he participated in private securities transactions without giving his member firm prior written notice of his intent to participate in such transactions and receiving approval for his participation. The findings stated that Rosenberg failed to respond to NASD requests for documents and information. **(NASD Case #E072004089701)**

Thomas Alfred Saunders (CRD #1362744, Registered Representative, Edgewater, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was censured, fined \$30,000, ordered to disgorge \$100,000 received from a securities account, and suspended from association with any NASD member

in any capacity for one month. Without admitting or denying the allegations, Saunders consented to the described sanctions and to the entry of findings that he gave authority to a registered representative at another member firm to trade shares of a security for the account including the time, price and amount of the trades. Through the other registered representative, the securities account engaged in transactions by which it purchased shares of the security and then sold the shares within 18 seconds at a price above the purchase price so that the account received approximately \$100,000 in profits as a result. The findings also stated that Saunders did not know the identities of the contra parties to the transactions that were executed through the other member firm.

Saunders' suspension began on March 6, 2006, and concluded at the close of business on April 5, 2006. (NASD Case #20050000350-02)

John Paul Schaffer (CRD #2139493, Registered Principal, Hazlet, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Schaffer consented to the described sanction and to the entry of findings that he converted \$74,000 from a public customer for his own use and benefit. The findings also stated that Schaffer failed to respond to NASD requests for information. (NASD Case #2005001551401)

Michael Ray Scheurich (CRD #2660521, Registered Representative, Boca Raton, Florida) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$7,500 and suspended from association with any NASD member in any capacity for five months. The fine must be paid before Scheurich reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Scheurich consented to the described sanctions and to the entry of findings that he settled a complaint directly with a public customer on the condition that the customer would retain Scheurich as the broker of record on her account, without informing his member firm. The findings stated that Scheurich guaranteed another public customer that her total account value would equal or exceed \$50,000, and that he would credit any deficiencies to the account.

Scheurich's suspension began on February 6, 2006, and will conclude at the close of business on July 5, 2006. (NASD Case #2005000163501)

Andrew Paul Schneider (CRD #2907279, Registered Representative, West Palm Beach, Florida) was fined \$5,000 and suspended from association with any NASD member in any capacity for 60 days. The National Adjudicatory Council (NAC) imposed the sanctions following appeal of an Office of Hearing Officers (OHO) decision. The sanctions were based on findings that Schneider engaged in outside business activities without providing prompt written notice to his member firm.

This action has been appealed to the SEC, and all sanctions are not in effect pending consideration of the appeal. (NASD Case #C10030088)

Blake Justin Shanaphy (CRD #3002887, Registered Representative, Hoboken, New Jersey) submitted an Offer of Settlement in which he was censured, fined \$5,000, suspended from association with any NASD member in any capacity for 45 days and barred from participating in, directly or indirectly, any public offering or transaction involving a penny stock. Without admitting or denying the allegations, Shanaphy consented to the described sanctions and to the entry of findings that, in connection with the purchase or sale of securities, and by the use of means or instrumentalities of interstate commerce, or by the mails, directly or indirectly, knowingly or recklessly, employed artifices, devices or schemes to defraud; made untrue statements of material facts or omitted to state material facts necessary in order to make the statements, in light of the circumstances under which they were made, not misleading; engaged in acts, practices or courses of business that operated or would operate as a fraud or deceit upon any person. The findings stated that Shanaphy recommended securities transactions and failed to furnish and obtain from the customers, prior to effecting such transactions, a signed risk disclosure document, failed to disclose and to provide to customers the inside bid and offer quotation and failed to keep and preserve records of such disclosures as required by the penny stock rules.

Shanaphy's suspension began on February 21, 2006, and will conclude at close of business on April 6, 2006. (NASD Case #CMS040165)

Ernie Preston Simmons, III (CRD #4728166, Registered Representative, Lititz, Pennsylvania) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Simmons consented to the described sanction and to the entry of findings that, while impersonating a public customer, he contacted an outside brokerage firm by telephone and requested the liquidation of the customer's account at such firm without the customer's authorization to do so. (NASD Case #2005002314501)

Anthony Paul Spinello (CRD #1961645, Registered Representative, Rochester, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Spinello consented to the described sanction and to the entry of findings that he converted \$127,950 from public customers without their knowledge, authorization or consent. The findings also stated that he failed to respond to NASD requests for information. (NASD Case #2005001826001)

Michael Adam Strulson (CRD #2677763, Registered Representative, Aston, Pennsylvania) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for three months. Without admitting or denying the allegations, Strulson consented to the described sanctions and to the entry of findings that he signed public customers' names on account opening agreements without their knowledge or consent.

Strulson's suspension began on March 6, 2006, and will conclude at the close of business on June 5, 2006. (NASD Case #E9A2004036901)

Ronald Mark Sussman (CRD #1932062, Registered Representative, Falls Church, Virginia) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Sussman consented to the described sanction and to the entry of findings that he charged a personal expense to a business credit card his member firm had issued to him for business use only, and

submitted a written request for reimbursement of the expense, representing it as business-related when he knew it was not. (NASD Case #2005002635301)

Anthony Peter Valois (CRD #2868602, Registered Principal, Staten Island, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000, barred from association with any NASD member in any principal or supervisory capacity, and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the allegations, Valois consented to the described sanctions and to the entry of findings that he failed to reasonably supervise registered representatives' activities, and failed to enforce his member firm's written supervisory procedures regarding heightened representative supervision and the handling of customer complaints.

Valois' suspension began on March 6, 2006, and will conclude at the close of business on April 4, 2006. (NASD Case #E062003011905)

Carl Van der Merwe (CRD #2561896, Registered Principal, Selah, Washington) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Van der Merwe consented to the described sanction and to the entry of findings that he created false and inaccurate books and records by falsifying expense reports reflecting \$96,000 in personal and duplicate expenditures as legitimate business expenditures, and provided violative gifts and gratuities to municipal bond traders and other employees of municipal securities broker-dealer firms with whom he conducted business. (NASD Case #EAF0301180001)

Donald Glenn Veltman (CRD #4646050, Registered Representative, Belding, Michigan) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Veltman consented to the described sanction and to the entry of findings that he received \$957 from a public customer for investment purposes and did not use the funds as the customer intended, thereby misusing the customer's funds. (NASD Case #E8A20040944-01)

Joseph David Wallwork (CRD #2833527, Registered Representative, Fairview, Pennsylvania) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Wallwork consented to the described sanction and to the entry of findings that he failed to respond to an NASD request to appear for an on-the-record interview. (NASD Case #2005000329601)

John Alan Wood (CRD #2490737, Registered Supervisor, Macon, Georgia) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for three months. The fine must be paid before Wood reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Wood consented to the described sanctions and to the entry of findings that he participated in outside business activities for compensation without providing written notice to his member firm.

Wood's suspension began on February 21, 2006, and will conclude on May 20, 2006. (NASD Case #2005002268201)

Individual Fined

James Geoffrey Morris (CRD #3075047, Registered Representative, Wyckoff, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was censured and fined \$15,000. The fine must be paid before Morris reassociates with any NASD member, or prior to any application or request for relief from any statutory disqualification. Without admitting or denying the allegations, Morris consented to the described sanctions and to the entry of findings that he prepared and submitted research reports containing price targets, research ratings and/or research summaries to companies whose equity securities were the subjects of the respective research reports, before publication of the reports and without providing complete drafts of them to his member firm. NASD found that Morris published research reports he had prepared and that did not disclose the valuation methods used to determine price targets contained within. (NASD Case #E1020020590-01)

Decisions Issued

The following decisions have been issued by the Office of Hearing Officers and has been appealed to or called for review by the NAC as of February 3, 2006. The findings and sanctions imposed in the decisions may be increased, decreased, modified, or reversed by the NAC. Initial decisions whose time for appeal has not yet expired will be reported in the next *Notice to Members*.

Charles James Cuozzo, Jr. (CRD #3123060, Registered Representative, Verona, New Jersey) was fined \$5,000 and suspended from association with any NASD member in any capacity for one year. The sanctions are based on findings that Cuozzo falsified information on customer annuity replacement forms on numerous occasions and forged a public customer's signature and initials without the customer's knowledge or consent.

The NAC has called this decision for review. The sanctions are therefore not in effect pending the consideration of the decision by the NAC. (NASD Case #C9B050011)

Dennis Todd Lloyd Gordon (CRD #1614614, Registered Principal, Rosenberg, Texas) and Sterling Scott Lee (CRD #1848950, Registered Principal, Austin, Texas) were barred from association with any NASD member in any capacity and ordered to pay \$22,657.40, plus interest, jointly and severally, in restitution to public customers. The sanctions were based on findings that Gordon and Lee permitted an unregistered individual who they knew, or should have known, was subject to a statutory disqualification to act as a member firm's principal for more than three years and for failing to disclose the individual's ownership or control of the firm to NASD. The findings stated that Gordon and Lee caused their member firm to charge markups in excess of 10 percent in transactions that were not fair and reasonable under the relevant circumstances nor disclosed in customer confirmations.

This decision has been appealed to the NAC, and the sanctions are not in effect pending consideration of the appeal. (NASD Case #C06040027)

Marylan Katherine Taylor (CRD #2263196, Registered Representative, Oval, Ohio) was barred by NASD in all capacities. The sanction was based on findings that Taylor falsified documents that included

completion certificates for continuing education courses, a beneficiary form change, and a Letter of Clearance and Certification from the Kentucky Department of Insurance and that Taylor failed to truthfully respond during an NASD on-the-record interview. NASD also found that Taylor failed to promptly amend her Form U4.

This decision has been appealed to the NAC, and the sanction is not in effect pending consideration of the appeal. (NASD Case #C8A050027)

Complaints Filed

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

Daniel Forrest Barrett (CRD #1789580, Registered Representative, Irving, Texas) was named as a respondent in an NASD complaint alleging that he made recommendations to a public customer to purchase high-risk stocks that were unsuitable for the customer based on the customer's age, financial status, investment objective and risk tolerance. The complaint also alleges that Barrett failed to respond to NASD requests to appear for an on-the-record testimony. (NASD Case #E062003043403)

Alexander M. Williams (CRD #3046599, Registered Representative, Brooklyn, New York) was named as a respondent in an NASD complaint alleging that he engaged in a level of trading in public customers' accounts that was excessive and unsuitable based on their financial circumstances and investment objectives. The complaint alleges that Williams received \$10,000 from a customer for investment purposes, but rather than invest all of the funds, he used \$6,000 for his own use and benefit without the customer's knowledge, authorization or consent. The complaint also alleges that Williams failed to respond to NASD requests for information. (NASD Case #E1020040687-01)

Firm Suspended Pursuant to NASD Rule 9553 for Failure to Pay Arbitration Fees

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

Morgan Wilshire Securities, Inc.
Westbury, NY
(January 30, 2006 to February 13, 2006)

Individual Barred Pursuant to NASD Rule 9552(h)

Jeffrey Marc Esposito, Sr.
Dallas, TX
(January 30, 2006)

Ellen Annette Guldenzopf
Portland, OR
(February 7, 2006)

Dennis Alvin Pearson, Jr.
San Diego, CA
(February 3, 2006)

Chris Michael Richardson
Sherwood, OR
(February 3, 2006)

Salvatore Michael Spadafora
Garden City, NY
(February 2, 2006)

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

Dmitry Gorodetsky
Brooklyn, NY
(January 27, 2006)

Joel Ellis Moskowitz
Boca Raton, FL
(January 27, 2006)

Scott Alan Webster
Riverview, FL
(January 13, 2006)

Individuals Suspended Pursuant to NASD Rule 9552(d)

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

Nathan Paul Araujo
West Palm Beach, FL
(January 17, 2006)

Fred Korahais
Glen Cove, NY
(January 17, 2006)

Peter Korahais
Glen Cove, NY
(January 17, 2006)

Sangam Ramesh Patel
San Jose, CA
(January 9, 2006)

Roy Roxton Smith, Jr.
Jonesboro, AR
(October 3, 2005)

Richard Wolfe Weinberg
Oxnard, CA
(February 6, 2006)

Emily Sun Wong
College Point, NY
(January 17, 2006)

Individuals Suspended Pursuant to NASD Rule Series 9554 for Failure to Comply with an Arbitration Award or a Settlement Agreement

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

Ellen Marie Aleshire
Antioch, IL
(February 22, 2006)

Marc Amato
Strongsville, OH
(February 28, 2006)

Gary Thomas Bolt
Myrtle Beach, SC
(January 19, 2006)

Wendy Purner Feldman
Rancho Santa Fe, CA
(February 9, 2006)

James Raymond Hamaker
Roanoke, TX
(February 22, 2006)

Paul Richard Hanson
Ft. Myers, FL
(January 19, 2006 to January 23, 2006)

Roderick Dylan Hudnell
Bartow, FL
(February 27, 2006)

Jeffrey Michael Hug
Aurora, CO
(January 19, 2006)

Phuong Lan Thi Huynh
San Deigo, CA
(February 9, 2006)

Sunny Michael Ikwue
Queens Village, NY
(January 18, 2006)

Shawn Michael Jeffcoat
Peidmont, OK
(January 10, 2006)

Stuart Neal Kingoff
Monsey, NY
(February 23, 2006)

Craig Leszczak
Hewlett, NY
(October 13, 2005 to February 6, 2006)

Robert Thomas Maloney
Buffalo, NY
(February 8, 2006)

Ronald Henry Mayfield
Spokane, WA
(February 8, 2006)

Todd Michael Newman
Royal Palm Beach, FL
(February 16, 2006)

Stephen Patrick
Atlanta, GA
(January 10, 2006)

Martin Harold Pesin
Nanuet, NY
(February 28, 2006)

Scott Michael Praizner
Sarasota, FL
(February 23, 2006)

Christopher Thomas Pyne
Philadelphia, PA
(February 13, 2006)

Jacqueline Quicksilver
Chesterfield, MO
(February 9, 2006)

Steve Paul Quinn
Littleton, CO
(January 19, 2006)

David Seth Samalin
Greenwich, CT
(February 22, 2006)

Walter Emil Weyrauch
Duluth, MN
(February 9, 2006)

Akhtar Uz Zaman
Aurora, IL
(January 17, 2006)

Sanford C. Bernstein & Co., Research Analyst Brad Hintz Fined \$550,000 for Violations of Research Analyst Conflict of Interest Rules

**Firm Developed Plan to Avoid Restriction on Stock
Sales by Analyst that Were Contrary to His
Published Recommendations**

NASD imposed a fine of \$350,000 against Sanford C. Bernstein & Co. LLC of New York and a fine of \$200,000 against Charles B. ("Brad") Hintz, one of the firm's research analysts, for violations of NASD's research analyst conflict of interest rules.

In its investigation, NASD found that Sanford Bernstein, a subsidiary of Alliance Capital Management L.P., had favorable ratings on Morgan Stanley and Lehman Brothers securities that remained in effect while its research analyst, Hintz, was selling his own shares in the two companies, a violation of NASD rules prohibiting trading contrary to an analyst's recommendation. Hintz also engaged in transactions in six securities held in a discretionary personal account that were contrary to his then-current recommendations.

The fines represent the largest NASD has imposed to date for violations of its new research analyst conflict of interest rules, which were first approved by the SEC on May 10, 2002 and went into effect beginning July 9, 2002.

"NASD's research analyst conflict of interest rules are designed to give customers confidence that analysts' stock recommendations are not biased due to any financial self-interest of the analyst," said James S. Shorris, Acting head of Enforcement. "Inconvenience or expense does not excuse non-compliance with NASD's rules against analysts trading contrary to their research recommendations."

NASD found that Hintz, a high profile analyst covering financial services companies, held a substantial amount of stock in Lehman Brothers and options to purchase stock in Morgan Stanley that he received as compensation when he served as the Chief Financial Officer and Treasurer, respectively, at those firms. Hintz's Morgan Stanley options were set to expire in January 2005. NASD found that Hintz wanted to sell his holdings in both companies to realize the substantial gain in the value of the securities and to diversify his portfolio. NASD rules, however, prohibit an analyst from

effecting stock transactions contrary to the analyst's current recommendations; Hintz had favorable ratings on both companies at the time.

In 2004, Sanford Bernstein—at Hintz's request—unsuccessfully sought an exemption from the rule prohibiting the sales, arguing that Hintz's circumstances constituted a "hardship" and that he should be allowed to sell his holdings. Thereafter, Sanford Bernstein developed a plan approved by the firm's legal and compliance department and senior management that it believed would allow Hintz to sell his holdings in Morgan Stanley and Lehman Brothers without violating NASD rules. Under this plan, Hintz issued what were purported to be his "final" reports on Morgan Stanley and Lehman on Dec. 23, 2004. Those reports rated the two companies "outperform" (the firm's highest rating) and "market-perform," respectively, and purportedly "terminated" coverage, while indicating that Hintz intended to resume coverage in February 2005 after selling all of his holdings in both companies. The reports further stated that the only "alternative" open to Hintz to allow him to sell his stock was to "terminate" coverage. One of the reports emphasized Hintz's purported dilemma by quoting Joseph Heller's *Catch-22*: "That's some catch, that Catch-22." To the contrary, Hintz did not have to sell his holdings and could have continued to hold his Morgan Stanley and Lehman Brothers securities, using other funds to pay for the costs of exercising his Morgan Stanley options.

Sanford Bernstein's plan did not comply with NASD rules. There was no bona fide termination of coverage because the firm intended to resume coverage of both stocks shortly after Hintz's stock sales were complete. The investment recommendations on both companies therefore remained in force, despite the purported "termination," and the stock sales in January 2005 violated NASD rules.

NASD also found that Hintz violated NASD rules as a result of numerous stock transactions in a discretionary brokerage account maintained at a domestic trust company. Sanford Bernstein, which received copies of the account statements, failed to supervise the activity in the discretionary account with a view towards preventing the violations. The account held securities in six companies that Hintz covered. Between August 2002 and January 2004, Hintz's discretionary account engaged in 27 transactions in those securities that

were contrary to his ratings. Also, 39 transactions were executed in the account either 30 days before or five days after Hintz published a research report on the company, thus violating NASD rules prohibiting transactions during a proscribed blackout period. In addition, between August 2002 and December 2003, Sanford Bernstein and Hintz did not disclose his holdings in these six securities in 60 research reports, as required by NASD rules.

In connection with these settlements, Sanford Bernstein and Hintz neither admitted nor denied the charges, but consented to the entry of NASD's findings.

NASD Orders Diversified Investors Securities to Pay Over \$2.2 Million for Facilitating Market Timing

Firm Also Fined for Supervisory Breaches, Email Failures

NASD fined Diversified Investors Securities Corp. of Purchase, NY, \$1.3 million for facilitating impermissible market timing by certain institutional and other customers in its Diversified Investors International Equity Fund. The firm must also pay nearly \$950,000 in restitution to the fund.

The settlement—the latest in a series of NASD enforcement actions involving impermissible market timing—also resolves related charges regarding email retention failures and supervisory breaches.

"What is troubling in this case is that, after the fund's prospectus was amended to put new restrictions in place specifically to discourage market timing, Diversified selectively permitted certain customers to carry out hundreds of market timing exchanges," said James Shorris, NASD Senior Vice President and Acting Head of Enforcement. "That special privilege was never disclosed to the fund's other shareholders, who were restricted from making frequent share exchanges."

Diversified is the principal underwriter and distributor of the Diversified Investors family of mutual funds, which are designed for retirement investing. Prior to June 2003, certain registered representatives at Diversified were aware that two groups of accounts had been opened for the purpose of market timing and had entered into agreements with Diversified Investment Advisors, Inc., the funds' investment advisor

and Diversified's parent company. The agreements permitted the accounts to market time, subject to certain restrictions.

While these market timing agreements were in place, language was added to the fund's prospectus informing investors that the fund had established new procedures designed to discourage large volume exchange activity that had the potential to affect negatively the fund and its other shareholders. The prospectus further stated that, effective June 30, 2003, if a shareholder sold fund shares, the shareholder may not be permitted to exchange shares back into the fund for 90 days. NASD found that despite these new prospectus restrictions, Diversified permitted the two groups of accounts with market timing agreements to continue their market timing activity. These accounts engaged in approximately 400 market timing round trip exchanges, purchasing and selling shares valued at over \$160 million from July through October 2003—disregarding the new prospectus trading restrictions, and in certain instances exceeding the trading limitations in their original market timing agreements.

NASD also found that while the prospectus limitations were not applied to the two groups of accounts with market timing agreements, approximately 80 letters were sent by a Diversified registered representative to other identified market timers, including investors who purchased and sold as little as \$5,000 per trade. Those investors were warned to cease market timing activity and were informed of the new prospectus language restricting an investor who sold interests in the fund from exchanging shares back into the fund for 90 days. However, these investors were not told that the new exchange restrictions were not being applied to the two groups of accounts with market timing agreements.

NASD also found that from November 2000 to December 2003, Diversified did not have an adequate system for retaining email communications and failed to ensure that emails were retained in accordance with record-keeping rules.

In settling with NASD, Diversified neither admitted nor denied the allegations, but consented to the entry of NASD's findings.

David Lerner Associates Suspended from Conducting New Business in Variable Annuities, Variable Life Insurance for 30 Days, Fined \$400,000 for Violations of New York State, NASD Regulations

Two Firm Principals Fined, Suspended for Supervision, Registration Violations

NASD fined Long Island, NY brokerage firm David Lerner Associates, Inc. \$400,000 and suspended the firm from engaging in any new variable life insurance or variable annuity business for 30 calendar days for engaging in replacement sales of variable life insurance and variable annuities that violated NASD and New York State rules. The suspension begins on March 20, 2006, and will conclude at the close of business on April 19, 2006.

NASD also fined and suspended two of the firm's principals. Martin Lerner, the firm's Executive Vice President of Sales, was suspended from acting in a supervisory capacity for 20 business days. Russell Moss, the firm's Assistant Vice President and Director of Insurance Services, was suspended in all capacities for 20 business days. Lerner and Moss were each held jointly and severally liable for \$25,000 of the fine against the firm. Both suspensions will begin on March 20, 2006, and will conclude at the close of business on April 7, 2006.

NASD found that between November 1998 and February 2004, David Lerner employees failed to comply with New York State Insurance Department Regulation 60 in connection with variable life insurance and variable annuity replacement sales. The regulation is aimed at ensuring that investors have full and clear information prior to making a decision to replace an existing insurance policy or annuity contract, and at reducing the opportunity for misrepresentations and incomplete comparisons in replacement situations. The circumvention of the New York State regulation also constitutes a violation of NASD rules requiring compliance with just and equitable principles of trade.

"New York's Regulation 60 is designed to protect investors from unsuitable recommendations by brokers to replace variable life and annuity contracts," said NASD Senior Vice President and Acting Head of Enforcement James Shorris. "It's intended to arm investors with the information they need about the

costs and other implications of making such replacements before their decision is final. The firm's routine circumvention of the regulation denied investors the required opportunities to fully consider and understand these important investment decisions."

Regulation 60 requires two separate interactions with a customer before a replacement can be completed. In step one, the customer is informed in writing—through a Definition of Replacement form—that a replacement is being considered. The customer must complete a Client Authorization form to allow the firm to collect information about the customer's existing life insurance policy or annuity contract, so that the customer will be able to make a meaningful comparison. Both forms must be signed and dated by the customer.

In step two, among other disclosures, the customer must be provided with a Disclosure Statement setting forth information comparing the old and new life insurance policies or annuity contracts, including the primary reason(s) for recommending the new policy or contract and the reason(s) why the existing policy or contract can no longer meet the applicant's objectives. The customer must sign and date an acknowledgement stating that the customer received and read the completed Disclosure Statement before signing the application for the new annuity contract or life insurance policy.

NASD's investigation showed that David Lerner's employees routinely circumvented the required Regulation 60 replacement process. NASD found that at their initial meetings with customers to discuss a potential variable life insurance or variable annuity replacement sale, the firm's employees routinely instructed customers to sign—but leave undated—all of the required step one and step two Regulation 60 documents. Subsequently, the David Lerner employees would forward the Regulation 60 documentation to an unregistered David Lerner employee in the firm's main office in Syosset, NY, who was responsible for processing all such paperwork.

That employee, with the knowledge of certain members of David Lerner management, routinely completed the required information on the pre-signed paperwork. This included filling in the necessary "Agent's Statement" on the Disclosure Statement, on which the representative

was required to list the primary reason(s) for recommending the new life insurance policy or annuity contract and why the existing life insurance policy or annuity contract could not meet the applicant's objectives. That employee completed the required Agent's Statement by consistently listing boilerplate information without having any direct knowledge or understanding of the reason for the proposed replacement in each particular case. Additionally, that employee, with the knowledge of certain members of the firm's management, routinely inserted fictitious dates on the pre-signed Regulation 60 documentation in order to create the false appearance that the required two-step procedure had been followed. The employee reviewed, completed, and processed all Regulation 60 documentation without any principal of the firm ever reviewing the documentation for compliance, as required by the regulation.

By having their clients during the initial meeting pre-sign undated and incomplete Regulation 60 documentation, David Lerner's sales force was in many instances able to effect variable life or variable annuity replacement sales before their clients ever received or reviewed the Regulation 60 documentation as completed by the unregistered employee at the firm's Syosset headquarters.

NASD found that during the relevant period, David Lerner effected at least 527 variable life insurance replacement sales to New York State residents and generated total revenue of more than \$3,431,000 from those sales. The firm also effected at least 259 variable annuity replacement sales to New York State residents and generated total revenue of more than \$1,372,000 from those sales during the relevant time period.

In addition to the Regulation 60 violations and related books and records violations, NASD also charged the firm, acting through Martin Lerner and Russell Moss, with failing to supervise the firm's sales force with a view towards preventing the Regulation 60 violations, as well as with registration violations for permitting Moss to function as a principal at the firm without being properly registered.

In concluding this settlement, David Lerner Associates, Lerner and Moss neither admitted nor denied the charges, but consented to the entry of NASD's findings.

David Lerner Associates was fined \$115,000 last September to settle charges of using misleading marketing materials with the public, including radio advertising, client seminars and other communications. In addition, the firm was ordered not to conduct any public seminars for 30 days. Earlier, NASD fined the firm \$100,000 for running improper sales contests to promote certain David Lerner proprietary mutual funds and selected variable annuity and variable life insurance products.