

NOVEMBER 2006

Notice to Members

Notices

- 06-61** SEC Approves Rule 3170 Requiring Members to Electronically File with or Otherwise Submit to NASD Specified Regulatory Notices or Other Documents; **Effective Date: December 6, 2006**
NASD Advises Firms That Certain Notices Required under the Securities Exchange Act of 1934 Must Be Filed Electronically Starting on January 1, 2007
- 06-62** SEC Approves Rule 3160 Regarding Submission and Reporting Requirements for Regulation T and SEC Rule 15c3-3 Extension of Time Requests; **Effective Date: March 1, 2007**
- 06-63** Amendments to Registration Rules Extending the Date by which Eligible Registrants must Complete Continuing Education Program before Engaging in Security Futures Activities; **Effective Date: November 15, 2006**
- 06-64** SEC Approves Amendments to Rule 10308 Regarding the Classification of Arbitrators; **Effective Date: January 15, 2007**
- 06-65** Securities Industry/Regulatory Council on Continuing Education Issues Firm Element Advisory
- 06-66** NASD Announces Election Results for District Committees, District Nominating Committees and the National Adjudicatory Council
- 06-67** SEC Approves Amendments to NASD Rules to Align Them with Regulation NMS; **Effective Date: Regulation NMS Trading Phase Date, Currently Scheduled to Occur February 5, 2007**

continued



06-68 SEC Approves Amendments to Rule 2340 to Allow DVP/RVP Customers to Elect Not to Receive Account Statements; **Effective Date: November 22, 2006**

Disciplinary and Other NASD Actions

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Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Legal & Compliance
Operations
Senior Management

KEY TOPICS

Electronic Filing Requirements
NASD Rule 3170

ACTION REQUIRED

Electronic Filing Requirements

SEC Approves Rule 3170 Requiring Members to Electronically File with or Otherwise Submit to NASD Specified Regulatory Notices or Other Documents; **Effective Date: December 6, 2006¹**

NASD Advises Firms That Certain Notices Required under the Securities Exchange Act of 1934 Must Be Filed Electronically Starting on January 1, 2007

Executive Summary

The Securities and Exchange Commission (SEC) has approved the adoption of NASD Rule 3170 (Mandatory Electronic Filing Requirements), which gives NASD the authority to require firms to file or submit electronically any regulatory notice or other document that a member is required to file with (or otherwise submit to) NASD.² **This Notice also advises firms that NASD will require certain notices required under the Securities Exchange Act of 1934 to be filed electronically starting on January 1, 2007.**

The effective date of this rule change is December 6, 2006. Included with this Notice is Attachment A, the text of Rule 3170.

Questions/Further Information

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

06-61

Adoption of Mandatory Electronic Filing Requirements under Rule 3170

Rule 3170 gives NASD authority to require firms to file or submit electronically any regulatory notice or other document that a member is required to file with (or otherwise submit to) NASD. NASD will issue a *Notice to Members* and other member communications, as appropriate, to advise its members as to each regulatory notice or document that members will be required to file with or submit in electronic format to NASD, and the date on which electronic filing or submission for these notices or documents will be required. NASD will also specify the electronic format to be used. These communications will advise members that as of the specified date, electronic filing or submission of the specified regulatory notices or documents will be mandatory, and NASD will no longer accept facsimile or other non-electronic transmissions of these notices or documents.³

NASD Announces New Electronic Filing Requirements Starting on January 1, 2007

Starting on January 1, 2007, NASD will require members to file electronically certain notices required to be filed under the Securities Exchange Act of 1934 (Exchange Act) via an electronic, Internet-based receiving and processing system (System), using templates developed by NASD for each notice.⁴ NASD members can access the templates for these regulatory notices on NASD's Web site. All members that file FOCUS reports will have access to the System, which will be available to members on NASD's Web site as part of NASD's infrastructure for Web-based regulatory form filing.⁵

Starting on January 1, 2007, the following notices must be filed with NASD electronically:

- ◆ Rule 15c3-1(e) Withdrawals of equity capital
- ◆ Rule 15c3-3(i) Special Reserve Bank Account
- ◆ Rule 17a-4(f)(2)(i);
Rule 17a-4(f)(3)(vii) Electronic storage media⁶
- ◆ Rule 17a-5(f)(4) Replacement of accountant⁷
- ◆ Rule 17a-11(b) Net capital deficiency
- ◆ Rule 17a-11(c)(1) Aggregate indebtedness is in excess of 1200 percent of net capital
- ◆ Rule 17a-11(c)(2) Net capital is less than 5 percent of aggregate debit items
- ◆ Rule 17a-11(c)(3) Net capital is less than 120 percent of required minimum dollar amount
- ◆ Rule 17a-11(d) Failure to make and keep current books and records
- ◆ Rule 17a-11(e) Material inadequacy in accounting systems, internal controls, or practices and procedures

Endnotes

- 1 Although this rule change becomes effective on December 6, 2006, members are not required to file electronically the notices specified in this Notice until January 1, 2007.
- 2 See Exchange Act Release No. 54654 (Oct. 26, 2006) (Order Approving Proposed Rule Change to Require Members to File Regulatory Notices with NASD Electronically; File No. SR-NASD-2006-060) (SEC Approval Order).
- 3 The notices required by SEC Rules 17a-4(f)(2)(i) and 17a-4(f)(3)(vii) (electronic storage media) and the notice required by SEC Rule 17a-5(f)(4) (replacement of accountant) require PDF attachments. Accordingly, NASD's Web site will advise firms that do not have access to PDF to contact NASD staff for alternate filing instructions.
- 4 Electronic filing of these notices with NASD does not affect requirements in those rules to file notices with the SEC or other securities regulatory agencies.
- 5 Currently, NASD members use this infrastructure to report, among other things, data required by Rule 3070 (reporting requirements), Rule 3150 (reporting requirements for clearing firms), Rule 3360 (short interest reporting), FOCUS reports as required by Exchange Act Rule 17a-5, and extension requests under Regulation T of the Federal Reserve Board and Exchange Act Rule 15c3-3.
- 6 See *supra* note 3.
- 7 See *supra* note 3.

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ATTACHMENT A

3100. BOOKS AND RECORDS, AND FINANCIAL CONDITION

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3170. Mandatory Electronic Filing Requirements

Each member shall be required to file with NASD, or otherwise submit to NASD, in such electronic format as NASD may require, all regulatory notices or other documents required to be filed or otherwise submitted to NASD, as specified by NASD.

* * * * *

Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Legal and Compliance
Senior Management
Operations
Extension of Time Requests

KEY TOPICS

NASD Rule 3160
Regulation T
SEC Rule 15c3-3

GUIDANCE

Extension of Time Requests

SEC Approves Rule 3160 Regarding Submission and Reporting Requirements for Regulation T and SEC Rule 15c3-3 Extension of Time Requests; **Effective Date: March 1, 2007**

Executive Summary

On September 15, 2006, the Securities and Exchange Commission (SEC) approved new NASD Rule 3160 that requires: (1) all clearing firm members for which NASD is the designated examining authority (DEA) pursuant to Rule 17d-1 under the Securities Exchange Act of 1934 (Exchange Act) to submit to NASD requests for extensions of time under Regulation T promulgated by the Federal Reserve Board (FRB) or pursuant to Rule 15c3-3(n) under the Exchange Act; and (2) each clearing firm member for which NASD is the DEA to file a monthly report with NASD indicating all broker-dealers for which it clears that have overall ratios of requested extensions of time to total transactions for the month that exceed 2%.¹

In addition, this *Notice* serves to remind members that extensions of time under Regulation T and SEC Rule 15c3-3 may only be requested in exceptional circumstances.

Rule 3160, as approved, is set forth in Attachment A of this *Notice*. The form of the new monthly report is set forth in Attachment B of this *Notice*. Rule 3160 will become effective on March 1, 2007.

Questions/Further Information

Questions regarding this *Notice* may be directed to Susan M. DeMando, Associate Vice President, Financial Operations, Member Regulation, at (202) 728-8411; or Kathryn M. Moore, Assistant General Counsel, Office of General Counsel, at (202) 974-2974.

Background and Discussion

Regulation T, issued by the Board of Governors of the FRB pursuant to the Exchange Act, among other things, governs the extension of credit to customers by broker-dealers for purchasing securities.² Rule 15c3-3 under the Exchange Act, among other things, requires broker-dealers to promptly obtain and maintain physical possession or control of customer securities and designates periods of time within which broker-dealers must cure any deficiency by buying-in or otherwise obtaining possession or control of the securities.³

Under SEC Rule 15c3-3(n), a self-regulatory organization (SRO) may extend certain specified periods to buy-in a security, for one or more limited periods commensurate with the circumstances, where the SRO: (1) is satisfied that the broker-dealer is acting in good faith in making the request; and (2) exceptional circumstances warrant such action.⁴ Regulation T has a similar standard to allow an extension of time for payment for purchases of securities.⁵

Required Submissions of Requests for Extensions of Time to the DEA

New Rule 3160(a) requires all clearing firm members for which NASD is the DEA to submit to NASD requests for extensions of time under Regulation T and SEC Rule 15c3-3(n).⁶ Since the SRO designated as a member's DEA has responsibility for examining its members for compliance with applicable financial responsibility rules such as Regulation T and SEC Rule 15c3-3, requiring a member to submit extension requests to its DEA helps to ensure that the DEA receives complete extension information to assist it in performing this function. This information, among other things, can serve as an early indicator of operational or other difficulties.

Monthly Reporting Requirement Regarding Introducing Firm Extensions

New Rule 3160(b) requires each clearing firm member for which NASD is the DEA to file a monthly report with NASD indicating all broker-dealers for which it clears (*i.e.*, introducing or correspondent firms) that have overall ratios of requests for extensions of time as contemplated by Sections 220.4(c) and 220.8(d) of Regulation T and SEC Rule 15c3-3(m)⁷ to total transactions for the month that exceed 2%.⁸ The monthly report will require clearing firms subject to Rule 3160(b) to identify, among other things: (1) the introducing broker-dealer's name; (2) the number of extension requests for the introducing broker-dealer for the calendar month; (3) the number of transactions for the introducing broker-dealer for the calendar month; and (4) the ratio of the number of extensions requested to total transactions.⁹ The monthly report must be submitted no later than five business days following the end of the preceding calendar month. For months when no introducing broker-dealer for which it clears exceeds the criteria, the clearing firm should submit a report indicating such.¹⁰

NASD has a new template within its electronic filing platform to permit clearing firms to submit the required reports regarding their introducing firms' extension requests. The form is set forth in Attachment B of this *Notice*.

Prohibition on Further Extensions when Thresholds are Exceeded

NASD will monitor the number of Regulation T and SEC 15c3-3 extension requests for each firm to determine whether to impose prohibitions on further extensions of time. As further detailed below, NASD will prohibit further extensions of time for introducing firms that exceed a 3% ratio of the number of extension requests to total transactions for the month (notwithstanding the fact that the monthly report described above identifies introducing firms that have ratios of extensions of time requests to total transactions exceeding 2% for the month).¹¹ In addition, NASD will prohibit further extensions of time for clearing firms that exceed a 1% ratio of extensions requested to transactions.¹²

More specifically, to the extent that firms exceed the applicable threshold limits (1% for clearing firms and 3% for introducing firms), NASD will inform them that their ability to receive extensions for their customers will be stopped for a 90-day period if the firm does not reduce the number of subsequent requests below the applicable limit by the next reporting period.¹³ NASD, however, will not prohibit further extensions of time for any introducing firm that engages in less than 25 transactions for the reported month. NASD believes that these limits are appropriate in light of the standard set forth in Regulation T and SEC Rule 15c3-3 that extensions of time may only be granted under "exceptional circumstances." While NASD does not at this time contemplate any changes to the thresholds referenced herein, any future changes to these parameters will be published in a subsequent *Notice to Members*.

Extension Requests Only in Exceptional Circumstances

As noted above, extensions of time under Regulation T and SEC 15c3-3 may only be requested in exceptional circumstances. When a firm requests an extension of time due to a customer failing to pay for securities purchases or to deliver securities sold, a written record of the contact with the customer regarding the transaction and the basis for requesting an extension must be retained. Without such documentation, members will not be in a position to demonstrate why exceptional circumstances existed to warrant the extension request. Members are reminded that NASD may review this documentation during the course of NASD examinations or may periodically request this documentation.

Customer Test Environment (CTE) Available

The requirements referenced in this *Notice* will become effective on March 1, 2007. However, to assist members in preparing to submit this additional report, NASD will provide a Customer Test Environment (CTE) available for testing purposes beginning on February 1, 2007. Member may access CTE at <https://regfilingtest.nasd.com>. To access CTE, a user will need to have a Regulation Filing Applications user ID and password. Questions regarding CTE may be directed to (800) 321-NASD.

Effective Date

As noted, for purposes of implementation of Rule 3160(a), if any member requests an extension of time under Regulation T or SEC Rule 15c3-3 on or after March 1, 2007, the member must submit the request to NASD if it is the firm's DEA. For purposes of implementation of Rule 3160(b), the member will submit its first report to NASD by April 6, 2007 (*i.e.*, within five business days of the end of the month) reflecting extensions to transactions for the month of March 2007; *i.e.*, March 1, 2007 through March 31, 2007.

Endnotes

- 1 See Exchange Act Release No. 54456 (September 15, 2006), 71 FR 56203 (September 26, 2006) (File No. SR-NASD-2006-064).
- 2 12 CFR 220.4(c) and 220.8(d). Regulation T provides that a customer has one payment period (currently five business days) to submit payment for purchases of securities in a cash account or in a margin account.
- 3 17 CFR 240.15c3-3.
- 4 See SEC Rule 15c3-3(n), authorizing SROs to extend the periods of time to buy-in a security specified in SEC Rules 15c3-3(d)(2), (d)(3), (h), and (m).
- 5 Under Regulation T, a firm's examining authority may grant an extension unless the examining authority believes that the broker-dealer is not acting in good faith or that the broker-dealer has not sufficiently determined that exceptional circumstances warrant such action.
- 6 This is consistent with the New York Stock Exchange (NYSE) Rule 434 which requires each firm for which the NYSE is the DEA to submit extensions of time requests to the NYSE.
- 7 SEC Rule 15c3-3(m) (Completion of Sell Orders on Behalf of Customers) requires that if a security sold long by a customer has not been delivered within 10 business days after the settlement date, the broker-dealer must either buy-in the customer or apply for and receive an extension from the SRO.
- 8 Self-clearing firms that do not also clear for other firms are not required to file these reports because such firms do not have any introducing broker extension information to provide to NASD.
- 9 Members should calculate the ratio by rounding to the nearest tenth of a percent. For example, if an introducing firm has 7 extension requests and 150 transactions in a calendar month, the ratio is equal to 4.7%.
- 10 See the report form set forth in Attachment B. For a report when one or more introducing firm(s) exceeds the 2% threshold for the reported month, the member should answer "yes" to the Data to File field. The member should complete the required information only for an introducing firm(s) that exceeded the 2% extensions to transactions ratio for the reported month. For a report where no introducing firm exceeds the 2% threshold, the member must still submit the report, however, the firm would answer "no" in the Data to File field.
- 11 The 2% threshold provides NASD with an "early warning" notice as to the concentrations of extension requests for introducing firms. NASD will use the information submitted by the clearing firms in the Rule 3160(b) monthly report to monitor introducing firms' compliance with the 3% threshold.

-
- 12 NASD will calculate the 1% ratio using the number of extensions requested pursuant to Regulation T and SEC Rule 15c3-3(m) to transactions as reported by the clearing firm on field 4980 of the FOCUS II Report.
- 13 For example, if an introducing firm exceeds the applicable threshold for the month of March 2007, its clearing firm would report that fact to NASD by April 6, 2007 (*i.e.*, the date that is five business days after the end of the month). NASD would advise the introducing firm that it had exceeded its threshold and that it must reduce the number of subsequent requests below the limit by the end of April 2007. If the introducing firm exceeds the applicable threshold for the month of April 2007, its clearing firm would report that fact to NASD by May 7, 2007 (*i.e.*, the date that is five business days after the end of the month) and the 90-day suspension would start at that time.

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ATTACHMENT A

New language is underlined.

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3160. Extensions of Time Under Regulation T and SEC Rule 15c3-3

(a) When NASD is the designated examining authority pursuant to SEC Rule 17d-1 for a member that is a clearing firm, such member must submit requests for extensions of time as contemplated by Sections 220.4(c) and 220.8(d) of Regulation T of the Federal Reserve Board and SEC Rule 15c3-3(n) to NASD for approval, in such format as NASD may require.

(b) Each member that is a clearing firm for which NASD is the designated examining authority is required to file a monthly report with NASD in such format as NASD may require, indicating all broker-dealers for which it clears that have overall ratios of requests for extensions of time as contemplated by Sections 220.4(c) and 220.8(d) of Regulation T of the Federal Reserve Board and SEC Rule 15c3-3(m) to total transactions for the month that exceed a percentage specified by NASD. The report is due to NASD within five (5) business days following the end of each reporting month.

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ATTACHMENT B

Reg-T & 15c3-3 [Cancel](#) [Help](#) [Logoff](#) [Home](#)

Active Filings
Submitted filings
Blank Forms
Monthly Filings
Draft Form
Submitted Reports
File Upload
Job Status

User Id: _____ **Firm Id:** _____

Request for Extension of Time Monthly Report

CRD Number : _____ Firm Name : _____
Month ending : _____ Contact Name : _____
Data to File : YES NO Contact Number : _____

The following broker-dealer(s) on whose behalf we carry accounts as correspondent have a ratio for the month of the number of extensions requested to total transactions exceeding two percent (2%).

[Click here to add](#) more row(s) [Check CRD ID](#)

CRD #	No of EXTN	No of Trans	Ratio	Correspondent's Name	Delete
0	0	0	0		✕
0	0	0	0		✕

[Click here to add](#) more row(s)

Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Legal & Compliance
Registered Representatives
Registered Principals
Senior Management
Continuing Education

KEY TOPICS

Rule 1022 (Categories of Principal Registration)
Rule 1032 (Categories of Representative Registration)
Security Futures

GUIDANCE

Security Futures Rules

Amendments to Registration Rules Extending the Date by which Eligible Registrants must Complete Continuing Education Program before Engaging in Security Futures Activities; **Effective Date: November 15, 2006**

Executive Summary

On October 16, 2006, NASD filed with the Securities and Exchange Commission (SEC) for immediate effectiveness a rule change to amend Rule 1022 (Categories of Principal Registration) and Rule 1032 (Categories of Representative Registration) to extend to December 31, 2009 the date by which all eligible registrants must complete a firm-element continuing education program to qualify to engage in security futures activities.¹ Rules 1022 and 1032, as amended, are set forth in Attachment A of this *Notice*. The implementation date of the amendments is November 15, 2006.

Questions/Further Information

Questions regarding this *Notice* may be directed to Patricia Albrecht, Assistant General Counsel, Office of General Counsel, at (202) 728-8026.

Discussion

In 2003, NASD modified the following registration categories to include the activities of engaging in and supervising securities futures: (1) Registered Options and Security Futures Principal (Series 4); (2) Limited Principal - General Securities Sales Supervisor (Series 9/10); (3) General Securities Representative (Series 7); and (4) Limited Representative - Options and Security Futures (Series 42). NASD also required that persons registered or becoming registered in these categories complete a firm-element continuing education requirement addressing security futures before conducting any security futures business.

NASD instituted this continuing education requirement to ensure that registered personnel, who may not be familiar with the risks, trading characteristics, terms and nomenclature of these products, or the fact that they are subject to the joint jurisdiction of the SEC and CFTC, receive appropriate training. The rules specified, however, that any person that intends to qualify to engage in security futures activities by completing a firm-element continuing education program must complete such program by December 31, 2006.

As noted in *Notice to Members 02-73* (November 2002), NASD initially considered creating new, or revising existing, qualification examinations for the registration categories listed above that would qualify a registrant to engage in security futures activities. The December 31, 2006 date was intended to be a cutoff date for existing registrants, who were qualified in a registration category for which a qualification examination was going to be created or revised, to complete the firm-element continuing registration requirement in lieu of taking the new or revised qualification examination.

However, there are no plans at present to create new or revised qualification examinations that would address security futures, and NASD believes that the continuing education requirement has been an effective method of ensuring that registered personnel are properly informed about security futures products. Accordingly, NASD has extended to December 31, 2009 the date by which all eligible registrants must complete a firm-element continuing education program to qualify to engage in security futures activities. Firms should be aware, however, that irrespective of the cutoff date, no eligible registrant may engage in any security futures business for which registration is required before completing the mandated firm-element continuing education requirement. The December 31, 2009 date serves merely as a cutoff date for eligible registrants to complete firm-element continuing education as an alternative to taking any new or revised qualification examinations addressing security futures that may be developed in the future.

The implementation date of the amendment is November 15, 2006.

Endnote

- 1 See Exchange Act Rel. No. 54617 (Oct. 16, 2006), 71 FR 62498 (Oct. 25, 2006) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Extend the Date by Which Eligible Registrants Must Complete Firm-Element Continuing Education to Qualify to Engage in a Securities Futures Business; SR-NASD-2006-118).

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ATTACHMENT A

New text is underlined; deletions are in brackets.

* * * * *

1022. Categories of Principal Registration

(a) through (e) No change.

(f) Limited Principal-Registered Options and Security Futures

(1) through (4) No change.

(5) Any person who is registered with NASD as a Registered Options and Security Futures Principal, or who becomes registered as a Registered Options and Security Futures Principal before a revised examination that includes security futures products is offered, must complete a firm-element continuing education program that addresses security futures and a principal's responsibilities for security futures before such person can supervise security futures activities. After a revised examination that includes security futures products is offered, a person associated with a member who passes such a revised Qualification Examination for Registered Options and Security Futures Principal (or any other examination covering security futures that is acceptable to NASD) is not required to complete a firm-element continuing education program that addresses security futures and a principal's responsibilities for security futures to supervise activities in such products, except as otherwise required by Rule 1120 generally or by the member firm. Any Registered Options and Securities Futures Principal who intends to qualify to supervise security futures activities by completing a firm-element continuing education program must complete such a program by December 31, 2009^[6]. Any Registered Options and Securities Futures Principal who has not completed a firm-element continuing education program by that date will be required to pass an appropriate qualification examination covering security futures to supervise security futures activities.

(g) Limited Principal-General Securities Sales Supervisor

(1) through (2) No change.

(3) Any person who is registered with NASD as a Limited Principal-General Securities Sales Supervisor, or who becomes registered as a Limited Principal-General Securities Sales Supervisor before a revised examination that includes security futures products is offered, must complete a firm-element continuing education program that addresses security futures and a principal's responsibilities for security futures before such person can supervise security futures activities. After a revised examination that includes security futures products is offered, a person associated with a member who passes such a revised Qualification Examination for Limited Principal-General Securities Sales Supervisor (or any other examination covering security futures that is acceptable to NASD) is not required to complete a firm-element continuing education program that addresses security futures and a principal's responsibilities for security futures to supervise such products, except as otherwise required by Rule 1120 generally or by the member firm. Any Limited Principal-General Securities Sales Supervisor who intends to qualify to supervise security futures activities by completing a firm-element continuing education program must complete such a program by December 31, 2009^[6]. Any Limited Principal-General Security Sales Supervisor who has not completed a firm-element continuing education program by that date will be required to pass an appropriate qualification examination covering security futures to supervise security futures activities.

(h) No change.

* * * * *

1032. Categories of Representative Registration

(a) General Securities Representative

(1) No change.

(2) Except as provided in Rule 1031(c):

(A) A person who is registered with the Association as a General Securities Representative, or who becomes registered as a General Securities Representative before a new examination that includes security futures is offered, must complete a firm-element continuing education program that addresses security futures products before such person can act as a General Securities Representative with regard to security futures products. After a new examination that includes security futures products is offered, a person associated with a member who passes such a new Qualification Examination for General Securities Representative (or any other examination covering security futures that is acceptable to NASD) is not required to complete a firm-element continuing education program that addresses security futures to act as a General Securities Representative with regard to such products, except as otherwise required by Rule 1120 generally or by the member firm. Once the new examination that includes security futures becomes available, persons seeking to become a General Securities Representative will be required to pass such new examination (or any other examination covering security futures that is acceptable to NASD) to act as a General Securities Representative with regard to security futures products. Only persons registered as a General Securities Representative prior to the time that the new examination is available ("eligible General Securities Representatives") will be eligible to use a firm-element continuing education program in lieu of passing the new examination or module to engage in a security futures business. Any eligible General Securities Representative who intends to qualify as a General Securities Representative with regard to security futures products by completing a firm-element continuing education program must complete such a program by December 31, 2009^[6]. Any eligible General Securities Representative who has not completed a firm-element continuing education program by that date will be required to pass an appropriate qualification examination to engage in security futures activities.

(B) through (D) No change.

(3) No change.

(b) through (c) No change.

(d) Limited Representative-Options and Security Futures

(1) through (3) No change.

(4) Any person who is registered with the Association as a Limited Representative-Options and Security Futures, or who becomes registered as a Limited Representative-Options and Security Futures before a revised examination that includes security futures is offered, must complete a firm-element continuing education program that addresses security futures. After a revised examination that includes security futures products is offered, a person associated with a member who passes such a revised Qualification Examination for Limited Representative-Options and Security Futures (or any other examination covering security futures that is acceptable to NASD) is not required to complete a firm-element continuing education program that addresses security futures to act as a limited representative with regard to such products, except as otherwise required by Rule 1120 generally or by the member firm. Any Limited Representative-Options and Security Futures who intends to qualify as a Limited Representative with regard to security futures products by completing a firm-element continuing education program must complete such a program by December 31, 2009^[6]. Any Limited Representative-Options and Security Futures who has not completed a firm-element continuing education program by that date will be required to pass an appropriate qualification examination covering security futures to engage in security futures activities.

(e) through (h) No change.

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Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Legal & Compliance
Arbitration

KEY TOPICS

Arbitrators
Dispute Resolution

GUIDANCE

Dispute Resolution

SEC Approves Amendments to Rule 10308 Regarding the Classification of Arbitrators; **Effective Date: January 15, 2007**

Executive Summary

The Securities and Exchange Commission has approved amendments to the arbitrator classification criteria set forth in Rule 10308 of the NASD Code of Arbitration Procedure (Code) to ensure that individuals with significant ties to the securities industry may not serve as public arbitrators in NASD arbitrations.¹

The text of the amendments is set forth in Attachment A. The amendments will be effective on January 15, 2007.

Questions/Further Information

Questions regarding this *Notice* may be directed to Barbara L. Brady, Vice President and Director of Neutral Management, at (212) 858-4352 or via email at barbara.brady@nasd.com; or John D. Nachmann, Counsel, at (202) 728-8273 or via e-mail at john.nachmann@nasd.com.

Discussion

The Code classifies arbitrators as public or non-public. When investors have a dispute with broker-dealer firms or their associated persons in NASD's arbitration forum, the investors are entitled to have their cases heard by an arbitration panel consisting of either a single public arbitrator or a majority public panel consisting of two public arbitrators and one non-public arbitrator, depending on the amount of the claim.²

Under Rule 10308(a)(4) of the Code, a person is classified as a non-public arbitrator if he or she:

(A) is, or within the past 5 years, was:

- (i) associated with a broker or a dealer (including a government securities broker or dealer or a municipal securities dealer);
- (ii) registered under the Commodity Exchange Act;
- (iii) a member of a commodities exchange or a registered futures association; or
- (iv) associated with a person or firm registered under the Commodity Exchange Act;

(B) is retired from, or spent a substantial part of a career, engaging in any of the business activities listed in subparagraph (4)(A);

(C) is an attorney, accountant, or other professional who has devoted 20 percent or more of his or her professional work, in the last two years, to clients who are engaged in any of the business activities listed in subparagraph (4)(A); or

(D) is an employee of a bank or other financial institution and effects transactions in securities, including government or municipal securities, and commodities futures or options or supervises or monitors the compliance with the securities and commodities laws of employees who engage in such activities.

The criteria for public arbitrators are set forth in Rule 10308(a)(5) of the Code. Under this rule, an individual will be classified as a public arbitrator if he or she is qualified to serve as an arbitrator and:

- (i) is not engaged in the conduct or activities described in paragraphs (a)(4)(A) through (D);
- (ii) was not engaged in the conduct or activities described in paragraphs (a)(4)(A) through (D) for a total of 20 years or more;
- (iii) is not an investment adviser;
- (iv) is not an attorney, accountant, or other professional whose firm derived 10 percent or more of its annual revenue in the past 2 years from any persons or entities listed in paragraph (a)(4)(A); and
- (v) is not the spouse or an immediate family member of a person who is engaged in the conduct or activities described in paragraphs (a)(4)(A) through (D).

In order to ensure that individuals with significant ties to the securities industry may not serve as public arbitrators in NASD arbitrations, NASD has amended the definition of public arbitrator in Rule 10308(a)(5) to exclude individuals who work for, or are officers or directors of, an entity that controls, is controlled by, or is under common control with, a partnership, corporation, or other organization that is engaged in the securities business.³ The revision to the rule also applies to individuals who have a spouse or immediate family member who works for, or is an officer or director of, an entity that is in such a control relationship with a partnership, corporation, or other organization that is engaged in the securities business.

Lastly, NASD has revised the definition of non-public arbitrator to clarify that persons who are registered through a broker-dealer may not be classified as public arbitrators. As noted above, arbitrators who are associated with a broker or dealer are considered non-public. In the financial services industry, it is not uncommon for a person to be employed by one company (such as a bank or insurance company) and to be registered to sell securities through another company (such as an affiliated broker-dealer). NASD believes that there may be some uncertainty among arbitrators who work for entities in a control relationship with a broker-dealer as to whether they are associated with a broker-dealer for purposes of Rule 10308, even though they hold licenses through the broker-dealer. Since the definition of "person associated with a member" in the NASD By-Laws includes persons who are registered with a broker-dealer, regardless of their status as employees, such persons should be considered non-public arbitrators. Therefore, NASD has amended the definition of non-public arbitrator in Rule 10308(a)(4)(A)(i) to clarify this issue.

Updating of Arbitrator Disclosures

NASD will distribute a survey to all arbitrators on the active roster, asking them to update their disclosures in light of the above amendments to the arbitrator classification rules. Arbitrators who do not respond by the deadline will be made inactive for future appointments until they have responded, and those who do not respond within a reasonable period thereafter may be removed permanently. After the surveys are returned and reviewed, arbitrators' disclosure records will be updated to reflect their proper classification under the amendments. Parties should be aware that the arbitrator classification amendments apply only to arbitrators appointed on or after the effective date; therefore, arbitrators who are already serving on panels may continue to serve even if their classification would otherwise change due to the amendments. These arbitrators will retain their former classification for purposes of these ongoing cases. This will avoid disruption and allow parties to continue with the arbitrators they have selected to hear their cases. Therefore, challenges for cause based solely on an arbitrator's reclassification will not be granted. Challenges for cause still may be made based upon the disqualification and removal criteria in Rules 10308(d) and 10312(d).

Effective Date

The amendments described in this *Notice* will be effective on January 15, 2007, and will apply to arbitrator lists sent out pursuant to Rule 10308(b)(5) on or after January 15, 2007, and to arbitrators appointed on or after January 15, 2007.

Endnotes

1. Securities Exchange Act Release No. 54607 (October 16, 2006), 71 *Federal Register* 62026 (October 20, 2006) (File No. SR-NASD-2005-094).
2. See Rules 10302 and 10308. For intra-industry disputes (not involving any parties who are investors) the panel composition is governed by Rule 10202. Depending on the nature of the dispute, intra-industry panels may consist of all public arbitrators, all non-public arbitrators or a majority of public arbitrators. The arbitrator classification provisions of Rule 10308 apply to all types of panels.
3. For purposes of this rule, the term "control" has the same meaning that it has for purposes of Form BD, which broker-dealers use to register with NASD and to make periodic updates. Specifically, control is defined as "[t]he power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. Any person that (i) is a director, general partner or officer exercising executive responsibility (or having similar status or functions); (ii) directly or indirectly has the right to vote 25% or more of a class of a voting security or has the power to sell or direct the sale of 25% or more of a class of voting securities; or (iii) in the case of a partnership, has the right to receive upon dissolution, or has contributed, 25% or more of the capital, is presumed to control that company." See Uniform Application for Broker-Dealer Registration (Form BD).

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ATTACHMENT A

New language is underlined; deletions are in brackets.

Code of Arbitration Procedure

* * * * *

Rule 10308. Selection of Arbitrators

(a) Definitions

(1) - (3) No change

(4) "non-public arbitrator"

The term "non-public arbitrator" means a person who is otherwise qualified to serve as an arbitrator and:

(A) is, or within the past 5 years, was:

(i) associated with, including registered through, a broker or a dealer (including a government securities broker or dealer or a municipal securities dealer);

(ii) registered under the Commodity Exchange Act;

(iii) a member of a commodities exchange or a registered futures association; or

(iv) associated with a person or firm registered under the Commodity Exchange Act;

(B) is retired from, or spent a substantial part of a career, engaging in any of the business activities listed in subparagraph (4)(A);

(C) is an attorney, accountant, or other professional who has devoted 20 percent or more of his or her professional work, in the last two years, to clients who are engaged in any of the business activities listed in subparagraph (4)(A); or

(D) is an employee of a bank or other financial institution and effects transactions in securities, including government or municipal securities, and commodities futures or options or supervises or monitors the compliance with the securities and commodities laws of employees who engage in such activities.

(5) "public arbitrator"

(A) The term "public arbitrator" means a person who is otherwise qualified to serve as an arbitrator and:

(i) is not engaged in the conduct or activities described in paragraphs (a)(4)(A) through (D);

(ii) was not engaged in the conduct or activities described in paragraphs (a)(4)(A) through (D) for a total of 20 years or more;

(iii) is not an investment adviser;

(iv) is not an attorney, accountant, or other professional whose firm derived 10 percent or more of its annual revenue in the past 2 years from any persons or entities listed in paragraph (a)(4)(A); [and]

(v) is not employed by, and is not the spouse or an immediate family member of a person who is employed by, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business;

(vi) is not a director or officer of, and is not the spouse or an immediate family member of a person who is a director or officer of, an entity that directly or indirectly controls, is controlled by, or is under common control with, any partnership, corporation, or other organization that is engaged in the securities business; and

(vii) is not the spouse or an immediate family member of a person who is engaged in the conduct or activities described in paragraphs (a)(4)(A) through (D).

(B) No change

(6) - (7) No change

(b) - (f) No change

* * * * *

Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Continuing Education
Legal & Compliance
Registration
Senior Management
Continuing Education

KEY TOPICS

Firm Element

GUIDANCE

Continuing Education

Securities Industry/Regulatory Council on Continuing Education Issues Firm Element Advisory

Executive Summary

The Securities Industry/Regulatory Council on Continuing Education (Council) has issued the annual Firm Element Advisory, a guide for firms to use when developing their continuing education Firm Element training plans. The Council suggests that firms use the Firm Element Advisory as part of the Firm Element Needs Analysis to help identify relevant training topics for all covered persons, including supervisors. Among the subjects you should consider for inclusion in Firm Element training are new rules and regulations, such as supervisory control amendments, business continuity plans and any new products or services the firm plans to offer.

This year the Firm Element Advisory has been redesigned to identify each topic briefly and then provide links to relevant documents issued on the specified subjects. Although the Firm Element Advisory is now designed for use on the Web, the document can be printed. The Firm Element Advisory can now be directly accessed at www.securitiescep.com/TOC/publications/FEA2006.pdf, or by going to the Council's Web site at www.securitiescep.com. Starting in 2007, the Council plans to update the Firm Element Advisory twice a year to provide firms with updated material.

In addition to the Firm Element Advisory material, the Council's Firm Element Organizer is a resource that can assist with developing Firm Element training plans. The Organizer is an easy-to-use software application that enables the search of an extensive database of regulatory resources related to specific investment products or services. The results of a search can then be edited into a document that may assist in developing a Firm Element training plan. The Firm Element Organizer also may be found on the Council's Web site.

Questions/Further Information

Questions concerning this *Notice* may be directed to Joseph McDonald, Associate Director, Testing and Continuing Education, at (240) 386-5065.

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Special Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Legal & Compliance
Operations
Registration
Senior Management

KEY TOPICS

District Elections

INFORMATIONAL

District and National Adjudicatory Council Elections

NASD Announces Election Results for District Committees, District Nominating Committees and the National Adjudicatory Council

Executive Summary

Through this *Notice*, NASD announces the election results for the District Committees, the District Nominating Committees and the National Adjudicatory Council (NAC). The candidates nominated to the District Nominating Committees have been duly elected in all districts. In the 11 District Committee elections, additional candidates satisfied the requirements of Article VIII of the NASD Regulation By-Laws to contest each District Committee election. The newly elected District Committee members will serve until January 2010,¹ and the newly elected District Nominating Committee members will serve until January 2008.

In the NAC elections, additional candidates satisfied the requirements of Article VI of the NASD Regulation By-Laws to contest two regional industry seats (New York and West) on the NAC. The individual who received the largest number of votes cast in the New York Region has been declared the nominee from that region. Similarly, the individual who received the largest number of votes cast in the West Region has been declared the nominee from that region. The Regional Nominating Committees for each region will nominate these individuals to the National Nominating Committee for appointment by the NASD Regulation Board.

The members of the incoming District Committees and District Nominating Committees, and the proposed NAC nominees, are identified in Attachment A. All petition candidates are identified as such. All other candidates were nominated by the District Nominating Committees.

06-66

Questions/Further Information

Questions concerning this *Notice* may be directed to the Regional or District Director noted in Attachment A or to Barbara Z. Sweeney, Senior Vice President and Corporate Secretary, NASD, at (202) 728-8062 or via email at barbara.sweeney@nasd.com.

Endnote

- 1 Some District Committee members were elected to fill existing vacancies and therefore may serve less than a three-year term, as indicated on Attachment A.

District 1

Debra J. Pohlson, Acting District Director

525 Market Street, Suite 300
San Francisco, CA 94105-2711

(415) 882-1200

Northern California (the counties of Monterey, San Benito, Fresno and Inyo, and the remainder of the state north or west of such counties), northern Nevada (the counties of Esmeralda and Nye, and the remainder of the state north or west of such counties) and Hawaii

District 1 Committee Incoming Members

Robert T. Angle <i>(petition candidate)</i>	White Pacific Securities, Inc.	San Francisco, CA
Leonard R. Berry	Backstrom McCarley Berry & Co., LLC	San Francisco, CA
James H. Williams	Financial Telesis, Inc.	San Rafael, CA

District 1 Nominating Committee Incoming Members

William A. Evans	Stone & Youngberg, LLC	San Francisco, CA
Gerard P. Gloisten	GBS Financial Corporation	Santa Rosa, CA
William P. Hayes	Wells Fargo Investments, LLC	San Francisco, CA
Francis X. Roche, II	RBC Dain Rauscher, Inc.	San Francisco, CA
William Svoboda	Morgan Stanley	Palo Alto, CA

District 2

Joseph M. McCarthy, Acting District Director

300 South Grand Avenue, Suite 1600
Los Angeles, CA 90071-3126

(213) 229-2300

Southern California (that part of the state south or east of the counties of Monterey, San Benito, Fresno and Inyo), southern Nevada (that part of the state south or east of the counties of Esmeralda and Nye) and the former U.S. Trust Territories

District 2 Committee Incoming Members

Craig M. Biddick <i>(petition candidate)</i>	Mission Securities Corporation	San Diego, CA
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Mark S. Stewart <i>(petition candidate)</i>	Mark Stewart Securities, Inc.	Irvine, CA
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Craig R. Watanabe	Western International Securities, Inc.	Pasadena, CA
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District 2 Nominating Committee Incoming Members

M. LaRae Bakerink	WBB Securities, LLC	San Diego, CA
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Stephen B. Benton	Financial Network Investment Corp.	El Segundo, CA
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Don S. Dalis	UBS Financial Services, Inc.	Newport Beach, CA
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James M. Dillahunty	Fixed Income Securities, LLC	San Diego, CA
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Neal E. Nakagiri	NPB Financial Group, LLC	Burbank, CA
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District 3

Joseph M. McCarthy, District Director

370 17th Street, Suite 2900
Denver, CO 80202-5629

(303) 446-3100

Arizona, Colorado, New Mexico, Utah and Wyoming

Michael E. Lewis, District Director

601 Union Street, Suite 1616
Seattle, WA 98101-2327

(206) 624-0790

Alaska, Idaho, Montana, Oregon and Washington

District 3 Committee Incoming Members

Chester J. Hebert	CIM Securities LLC	Greenwood Village, CO
James W. Millegan <i>(petition candidate)</i>	J.W. Millegan, Inc.	Oswego, OR
Douglas W. Schriener <i>(petition candidate)</i>	Harrison Douglas, Inc.	Aurora, CO

District 3 Nominating Committee Incoming Members

Bridget Gaughan	AIG Financial Advisors, Inc.	Phoenix, AZ
John Goodwin	Goodwin Browning & Luna Securities, Inc.	Albuquerque, NM
Curtis Hammond	Morgan Stanley DW Inc.	Bellevue, WA
J. Keith Kessel	AFS Brokerage, Inc.	Greenwood Village, CO
Arlene Wilson	D.A. Davidson	Great Falls, MT

District 4

Thomas D. Clough, District Director

120 West 12th Street, Suite 800
Kansas City, MO 64105-1930

(816) 421-5700

Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota and South Dakota

District 4 Committee Incoming Members

Kenneth M. Cherrier ¹	Fintegra, LLC	Minneapolis, MN
Robert E. Hillard <i>(petition candidate)</i>	Arlington Securities, Inc.	St. Louis, MO
Richard D. Link	Edward Jones	St. Louis, MO
Daniel J. May	Financial Network Investment Corporation	Minneapolis, MN

District 4 Nominating Committee Incoming Members

Robert M. Chambers	A.G. Edwards & Sons, Inc.	West Des Moines, IA
Joseph D. Fleming	RBC Dain Rauscher Inc.	Minneapolis, MN
Mark T. Lasswell	Wells Fargo Brokerage Services, LLC	Minneapolis, MN
Kevin P. Maas	PrimeVest Financial Services, Inc.	St. Cloud, MN
Stephen S. Soden	Country Club Financial Services, Inc.	Mission Woods, KS

¹ Mr. Cherrier has been elected to serve the remaining year of the term of Stephen R. Oliver, who resigned from the District Committee.

District 5

Keith E. Hinrichs, District Director

1100 Poydras Street, Energy Center, Suite 850
New Orleans, LA 70163-0802

(504) 522-6527

Alabama, Arkansas, Louisiana, Mississippi, Oklahoma and Tennessee

District 5 Committee Incoming Members

Robert Keenan, Jr. <i>(petition candidate)</i>	St. Bernard Financial Services, Inc.	Russellville, AR
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Michael J. Mungenast	ProEquities, Inc.	Birmingham, AL
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Gary K. Wunderlich, Jr.	Wunderlich Securities, Inc.	Memphis, TN
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District 5 Nominating Committee Incoming Members

John J. Dardis	Next Financial Group, Inc.	Metairie, LA
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Henry M. Fyfe, III	Duncan-Williams, Inc.	Memphis, TN
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Charles C. Hollinger, Jr.	Johnson Rice & Company, LLC	New Orleans, LA
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Carolyn R. May	Simmons First Investment Group, Inc.	Little Rock, AR
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R. Patrick Shepherd	Avondale Partners, LLC	Nashville, TN
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District 6

Virginia F. M. Jans, Regional Director

12801 N. Central Expressway, Suite 1050
Dallas, TX 75243-1778

(972) 701-8554

Texas

District 6 Committee Incoming Members

Caroline B. Austin <i>(petition candidate)</i>	Evolve Securities, Inc.	Dallas, TX
Kennard (Ken) R. George	VSR Financial Services, Inc.	Dripping Springs, TX
Fenner R. Weller, Jr.	Weller Anderson & Co., Ltd.	Houston, TX

District 6 Nominating Committee Incoming Members

Karen Banks	Frost Brokerage Services, Inc.	San Antonio, TX
Cynthia E. Besek	Maplewood Investment Advisors, Inc.	Dallas, TX
William D. Felder	Southwest Securities, Inc.	Dallas, TX
Brent T. Johnson	Multi-Financial Securities Corporation	Houston, TX
John R. Muschalek	First Southwest Company	Dallas, TX

District 7

Daniel J. Stefek, District Director

One Securities Center, Suite 500
3490 Piedmont Road, NE
Atlanta, GA 30305-4808

(404) 239-6100

Georgia, North Carolina and South Carolina

Mitchell C. Atkins, District Director

2500 N. Military Trail, Suite 302
Boca Raton, FL 33431-6324

(561) 443-8000

*Florida, Puerto Rico, the Canal Zone and
the Virgin Islands*

District 7 Committee Incoming Members

Jed E. Bandes	Mutual Trust Co. of America Securities	Clearwater, FL
Valerie G. Brown	ING Financial Partners, Inc.	Atlanta, GA
Karen Z. Fischer <i>(petition candidate)</i>	Hunter Scott Financial LLC	Delray Beach, FL
Raymond H. Smith, Jr. ²	Smith, Brown & Groover, Inc.	Macon, GA

District 7 Nominating Committee Incoming Members

Susan J. Hechtlinger	Banc of America Investment Services, Inc.	Charlotte, NC
Landrum H. Henderson, Jr.	Stephens, Inc.	Charlotte, NC
Dennis S. Kaminski	Mutual Service Corporation	West Palm Beach, FL
James A. Klotz	FMSBonds, Inc.	North Miami Beach, FL
Alan L. Maxwell	Wachovia Capital Markets, LLC	Charlotte, NC

² Mr. Smith has been elected to serve the remaining year of the term of Erick R. Holt, who resigned from the District Committee.

District 8

Carla A. Romano, Regional Director

55 West Monroe Street, Suite 2700
Chicago, IL 60603-5052

(312) 899-4400

Illinois, Indiana, Kentucky, Michigan, Ohio and Wisconsin

District 8 Committee Incoming Members

Joel R. Blumenschein	Freedom Investors Corp.	Hartland, WI
Thomas A. Bono	David A. Noyes & Company	Oak Park, IL
Steven J. Greenwald	Telemus Investment Brokers, LLC	Southfield, MI

District 8 Nominating Committee Incoming Members

George E. Bates	Bates Securities, Inc.	Rockford, IL
Michael E. Bosway	City Securities Corporation	Indianapolis, IN
Mari Buechner	Coordinated Capital Securities, Inc.	Madison, WI
Ruth C. Hannenberg	Mesirow Financial, Inc.	Chicago, IL
Robert J. Michelotti	Ferris, Baker Watts Incorporated	Auburn Hills, MI

District 9

Gary K. Liebowitz, Regional Director

581 Main Street, 7th Floor
Woodbridge, NJ 07095-1164

(732) 596-2000

New Jersey and New York (except for the counties of Nassau and Suffolk, and the five boroughs of New York City)

Robert B. Kaplan, District Director

1835 Market Street, Suite 1900
Philadelphia, PA 19103-2929

(215) 963-1992

Delaware, the District of Columbia, Maryland, Pennsylvania, Virginia and West Virginia

District 9 Committee Incoming Members

Wayne F. Holly	Sage, Ruty & Co., Inc.	Rochester, NY
Richard P. Seelaus <i>(petition candidate)</i>	R. Seelaus & Co., Inc.	Summit, NJ
Timothy L. Smith	Comprehensive Asset Management and Servicing, Inc.	Parsippany, NJ

District 9 Nominating Committee Incoming Members

A. Louis Denton	Peterson Investments, Inc.	Blue Bell, PA
Peter P. Jenkins	Credit Suisse Securities (USA) LLC	Baltimore, MD
W. Dean Karrash	Burke, Lawton, Brewer & Burke	Spring House, PA
Gregg A. Kidd	Pinnacle Investments Inc.	East Syracuse, NY
Harold N. Peremel	Mercantile Brokerage Services, Inc.	Baltimore, MD

District 10

Hans L. Reich, Regional Director

165 Broadway, 52nd Floor
New York, NY 10006-1400

(212) 858-4000

New York (the counties of Nassau and Suffolk, and the five boroughs of New York City)

District 10 Committee Incoming Members

James A. Brodie, Jr. <i>(petition candidate)</i>	Carr Securities Corporation	Port Washington, NY
Kathryn G. Casparian	CIBC World Markets Corp.	New York, NY
Paul S. Ehrenstein <i>(petition candidate)</i>	Zenith American Securities Corporation	New York, NY
Craig B. Jampol ³	Caris & Company	New York, NY
James D. Lamke	Bear Stearns & Co. Inc.	New York, NY

District 10 Nominating Committee Incoming Members

Margaret M. Caffrey	Schonfeld & Company, LLC	Jericho, NY
Lon T. Dolber	American Portfolios Financial Services, Inc.	Holbrook, NY
George T. Mimura	Nomura Securities International, Inc.	New York, NY
Richard J. Paley	Carey Financial Corporation	New York, NY
Howard R. Plotkin	Lehman Brothers Inc.	New York, NY

3 Mr. Jampol has been elected to serve the remaining year of the term of Jeffrey T. Letzler, who resigned from the District Committee.

District 11

Frederick F. McDonald, District Director

99 High Street, Suite 900
Boston, MA 02110

(617) 532-3400

Connecticut, Maine, Massachusetts, New Hampshire, Rhode Island and Vermont

District 11 Committee Incoming Members

Michael E. Callaghan	Harvest Capital LLC	Wethersfield, CT
Tina Blakeley Maloney <i>(petition candidate)</i>	Winslow, Evans & Crocker, Inc.	Boston, MA
Therese M. Squillacote	ING Financial Advisers, LLC	Hartford, CT

District 11 Nominating Committee Incoming Members

David K. Booth	Jefferson Pilot Securities Corp.	Concord, NH
Mark R. Hansen	Alta Capital Group, LLC	Boston, MA
Thomas F. Hollenbeck	National Financial Services, LLC	Wellesley Hills, MA
Wilson G. Saville	Barrett & Company	Providence, RI

National Adjudicatory Council – New York Region Seat

Samuel F. Lek
(petition candidate)

Lek Securities Corporation

New York, NY

National Adjudicatory Council – West Region Seat

David P. Alsup
(petition candidate)

North American Clearing, Inc.

Laguna Hills, CA

Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Legal & Compliance
Operations
Registered Representatives
Senior Management
Systems
Trading

KEY TOPICS

ADF Trading Centers
Alternative Display Facility (ADF)
Regulation NMS
Trade Reporting

GUIDANCE

Alignment of NASD Rules with Regulation NMS

SEC Approves Amendments to NASD Rules to Align Them with Regulation NMS; **Effective Date: Regulation NMS Trading Phase Date, Currently Scheduled to Occur February 5, 2007**

Executive Summary

On September 28, 2006, the Securities and Exchange Commission (Commission or SEC) approved amendments to NASD Rules, including the rules governing the Alternative Display Facility (ADF),¹ in order to align them with Regulation NMS.² In addition, the SEC approved amendments to rules governing quoting, trade reporting, and clearing applicable to the ADF and extended this functionality to all NMS stocks, including stocks listed on the New York Stock Exchange (NYSE), American Stock Exchange (Amex), and certain other exchanges. Furthermore, the amendments reorganize ADF trade reporting rules and make changes to ADF rules to enhance their clarity. The SEC also approved changes to the ADF Trading Center Certification Record, which became effective upon SEC approval on September 28, 2006.

The Rules, as amended (See Exhibit 5 of the rule filing), and the ADF Trading Center Certification Record (See Exhibit 3 of the rule filing) are available at www.nasd.com/RulesRegulation/RuleFilings/2006RuleFilings/NASDW_017057. The amendments to NASD Rules become effective on the Regulation NMS Trading Phase Date, currently scheduled to occur on February 5, 2007.

Questions/Further Information

Questions concerning this *Notice* may be directed to Kathleen A. O'Mara, Associate General Counsel, Office of General Counsel, at (202) 728-8071; Peter Santori, Chief Counsel, Market Regulation Department, at (240) 386-5126; or Chris Stone, Associate Chief Counsel, Transparency Services, at (202) 728-8457.

06-67

Background and Discussion

On June 29, 2005, the Commission published its release adopting Regulation NMS.³ Regulation NMS established substantive rules designed to modernize and strengthen the regulatory structure of the U.S. equities markets. For example, the Order Protection Rule (SEC Rule 611) requires “trading centers” to establish, maintain and enforce written policies and procedures reasonably designed to prevent the execution of trades at prices inferior to protected quotations displayed by automated trading centers, subject to applicable exceptions.⁴ For trades to be protected, a quotation must be immediately and automatically accessible. In this regard, Regulation NMS includes an Access Rule (SEC Rule 610), which requires fair and non-discriminatory access to quotations, establishes a limit on access fees to harmonize the pricing of quotations across different trading centers, and requires NASD and the exchanges to establish, maintain and enforce written rules that prohibit their members from engaging in a pattern or practice of displaying any quotation that locks or crosses a protected quotation, or a manual quotation that locks or crosses a quotation disseminated pursuant to an effective National Market System Plan (NMS Plan).⁵

Aligning NASD Rules with Regulation NMS

NASD is amending its ADF Rules to align them with the Regulation NMS Order Protection Rule and the Access Rule. NASD also is making conforming changes to certain NASD Rules to reflect the new numbering of SEC Rules in Regulation NMS. Moreover, NASD has filed its ADF Trading Center Certification Record with the SEC. ADF Trading Centers are required to complete the ADF Trading Center Certification Record, provide all relevant supporting documentation and complete the ADF certification process prior to being permitted to post quotations through the ADF.

1. Implementation of the Order Protection Rule

Consistent with the goals articulated by the Commission in adopting SEC Rule 611, NASD is amending Rule 4300A(e) to specify that an ADF Trading Center must submit automated quotations, as defined in SEC Rule 600(b)(3). Under Rule 4300A(e), manual quotations, as defined in SEC Rule 600(b)(37), cannot be submitted to the ADF. In furtherance of the provision, Rule 4300A(e) requires that each ADF Trading Center adopt policies and procedures to ensure only automated quotations are submitted to the ADF. Moreover, an ADF Trading Center is required to monitor its systems on a real-time basis to assess whether they are functioning properly.

NASD also is amending the system outage procedures in Rule 4300A. A system outage now is defined in Rule 4300A(e)(2) as the inability to post automated quotations in the ADF⁶ and, in that regard, the inability to respond immediately and on an automated basis to orders. In light of the time frames that are pertinent in the Regulation NMS environment, NASD is amending Rule 4300A to address ADF Trading Center system outages. NASD will determine, in its discretion: (1) when three unexcused outages during a five-day period should result in the suspension of an ADF Trading Center from quoting in the ADF for a period of 20 days; and (2) whether an outage should be excused without limitation.⁷ NASD will strictly interpret the requirement under Rule 4300A that an ADF Trading Center submit only automated quotations. Moreover, if an ADF Trading Center experiences technical problems and is unable to submit automated quotations, it will have to withdraw its quotations from the ADF and notify NASD.

NASD also is amending ADF transaction reporting requirements to expressly require reporting members to append certain new identifiers to enhance regulation of the Order Protection Rule and to facilitate transparency to the marketplace. There are nine express exceptions in the Order Protection Rule.⁸ NASD is revising its transaction reporting requirement in Rule 4632A to conform NASD trade report modifiers to the identified exceptions in SEC Rule 611.⁹ Specifically, NASD is adopting a new unique trade report modifier that will be appended to a last sale report if the trade would be a trade-through of a protected quotation, but for the trade being qualified for an exception from SEC Rule 611. Furthermore, in addition to using the new unique identifier, reporting members are required to append an additional modifier, specified by NASD, which would, in certain circumstances, identify the specific applicable exception or exemption from SEC Rule 611 upon which the member is relying. Moreover, NASD plans to issue another *Notice* providing further guidance on Regulation NMS-related trade reporting requirements.

In addition, NASD is amending Rule 4632A to require separate trade report modifiers for certain trading situations that previously had been combined under one modifier. Additionally, NASD is creating several new trade report modifiers to supplement the amended modifiers. ADF order reporting requirements in Rule 4300A(b)(1)(N) and transaction reporting requirements in Rule 4632A(a)(4)(L) were amended to expressly require the reporting of "[a]ny other modifier as specified by NASD or the Securities and Exchange Commission." Further, NASD provided a comprehensive list of all required modifiers when it published ADF's technical specifications on October 16, 2006. The list is available at www.nasd.com/RegulatorySystems/ADF/FIX/Information/index.htm.

NASD will review the activities of ADF Trading Centers and other NASD member trading centers for compliance with the Order Protection Rule.¹⁰ To complement NASD's automated surveillance for member compliance with the Order Protection Rule and other NASD surveillance methods, NASD's Trading and Market Making Surveillance (TMMS) examination program will examine relevant NASD members for adequate written supervisory procedures and supervisory systems applicable to Regulation NMS and to determine the extent to which trading centers are reviewing compliance with such rules.

2. Implementation of the Access Rule

The Access Rule promotes fair and non-discriminatory access to quotations displayed by trading centers through a private linkage approach. In general, the Access Rule: (1) requires that self-regulatory organizations (SROs) not impose unfairly discriminatory terms that prevent or inhibit any person from obtaining efficient access through a member to the quotations in an NMS stock displayed through its SRO trading facility; (2) requires that each trading center that displays quotations in an NMS stock through an SRO display-only facility (such as the ADF) provide a level and cost of access to such quotations that is substantially equivalent to the level and cost of access to quotations displayed by SRO trading facilities in that stock and ensure that it does not impose unfairly discriminatory terms that prevent or inhibit any person from obtaining efficient access to such quotations through a member, subscriber or customer of the trading center; (3) adopts limits on fees for accessing quotations; and (4) requires SROs to establish, maintain and enforce specific written rules that are generally aimed at limiting the display of quotations that lock or cross any protected quotations in an NMS stock.

In approving Regulation NMS, the Commission articulated the expectation that NASD, as the SRO responsible for the OTC market, will act as “gatekeeper” of the ADF.¹¹ In that regard, NASD will have to make an “affirmative determination” as to whether ADF Trading Centers are complying with the SEC Rule 610 access standard.¹² NASD will fulfill this obligation in several ways. First, NASD is incorporating the Regulation NMS access standard into Rule 4300A. An ADF Trading Center will be expressly required to: (1) provide a level and cost of access to its quotations in an NMS stock displayed in the ADF that is substantially equivalent to the level and cost of access to quotations displayed by SRO trading facilities in that NMS stock; (2) demonstrate that it has sufficient technology to update automatically its quotations and immediately respond to orders routed for execution directly against the individual ADF Trading Center’s best bid or offer (i.e., sufficient technology to display automated quotations); and (3) ensure that it does not impose unfairly discriminatory terms that prevent or inhibit any person, through a registered broker-dealer, from obtaining efficient access to such quotations. Further, NASD is amending Rule 4300A to require ADF Trading Centers to provide direct electronic access to registered broker-dealers seeking such access.¹³

Based on guidance provided by Commission staff, Rule 4300A(d)(1) is being amended to require each ADF Trading Center to use a communication service(s) that is deemed sufficient by NASD. To facilitate this effort, NASD staff has posted on the NASD Web site a list of NASD-approved private-sector connectivity providers (e.g., financial extranet services and direct market access firms). The list of providers is available at www.nasd.com/RegulatorySystems/ADF/Participants/index.htm. This list will be reviewed periodically and updated on an as-needed basis. As stated in the rule filing, NASD staff will not necessarily review the technical functionality of the various connectivity providers, but will assess the reliability, cost effectiveness, and extent to which the service is sufficiently prevalent among firms that require the ability to route orders to an ADF Trading Center to meet their Order Protection Rule obligations.

In addition, while NASD staff will evaluate the level and cost of accessing an ADF Trading Center on a case-by-case basis, each ADF Trading Center is required to be accessible through at least two approved connectivity providers. It is important to note, however, that the approved private-sector connectivity provider list does not serve as an exclusive list of connectivity options for accessing an ADF Trading Center. For instance, an ADF Trading Center could approach NASD about adding a specific private-sector connectivity provider to the approved list that is not currently listed. In addition, to the extent a market participant deems it necessary, it could choose to connect to an ADF Trading Center via a dedicated telecommunications line. However, an ADF Trading Center will not be obligated to provide such dedicated access if it is accessible through at least two providers on the approved list. Also, in conformity with the guidance provided by the Commission in the Regulation NMS Approval Order, NASD expects an ADF Trading Center to defray connectivity costs to the extent that the level and cost of access offered by the ADF Trading Center is not substantially equivalent to the level and cost of access offered generally by SRO trading facilities.¹⁴

Second, NASD is amending its Certification Record process to address the standards set forth in SEC Rule 610 and Regulation NMS generally, including requiring documentation that demonstrates that ADF Trading Center costs are substantially equivalent to the costs of accessing SRO trading facilities generally.¹⁵ The Certification Record process will specifically require each ADF Trading Center to make fully supported representations that it is able to comply with the various requirements of Regulation NMS. To that end, one of the goals of NASD's amended Certification Record process is to make certain that ADF Trading Centers possess technology capable of offering automated quotations (*i.e.*, that ADF Trading Centers are capable of immediate internal order turnaround times). The Commission has tasked NASD with making an affirmative determination as to the extent to which each ADF Trading Center offers a substantially equivalent level and cost of access relative to SRO trading facilities. This requires NASD staff to consider the ADF Trading Center's system functionality, robustness, the ability of market participants to interface efficiently with the ADF Trading Center's system and the fee structure of the ADF Trading Center.

Third, NASD is amending Rule 4400A to provide standing for all registered broker-dealers, not just members, to file a direct or indirect access complaint with NASD. This will ensure that there is a process in place for promptly addressing claims that an ADF Trading Center is preventing or inhibiting efficient access to its quotations.¹⁶ NASD will allow such complaints to be filed via facsimile, email, personal delivery, courier or overnight mail. Moreover, the process specified in Rule 4400A will allow NASD to promptly address such issues and, if it were determined that there has been or were an ongoing limitation or denial of access, NASD will limit, as appropriate and necessary, an ADF Trading Center's participation in ADF, including the withdrawal of its quotations from ADF, until access is provided.¹⁷

Fourth, through the examination process and annual compliance questionnaires, NASD will review the activities of ADF Trading Centers. With regard to the Access Rule, NASD's automated surveillance for certain aspects of the Access Rule will be complemented through the review of relevant NASD members' written supervisory procedures through the TMMS examination program, among other investigative means. NASD also plans to use annual compliance questionnaires to determine ongoing compliance with requirements such as "substantially equivalent" access, access fees and conditions on access.

Lastly, in adopting Rule 4130A (Prohibition from Locking or Crossing Quotations in NMS Stocks), NASD is requiring members to reasonably avoid displaying, and expressly prohibiting members from engage in a pattern or practice of displaying, any quotation that locks or crosses a protected quotation in an NMS stock during regular trading hours, unless it meets a specified exception, and to avoid displaying a manual quotation that locks or crosses any quotation in an NMS stock previously disseminated pursuant to an effective NMS Plan.¹⁸ Commission staff asked each of the SROs to ensure that its locking or crossing quotation rules are generally consistent among the SROs. Accordingly, new Rule 4130A is adopted in conformity with the SRO requirements set forth in the Access Rule. Further, NASD is amending Rule 4613A to delete provisions that currently prohibit locked or crossed intra-market quotations during regular trading hours. New Rule 4130A will now be applied during regular market hours, rather than Rule 4613A. However, the provisions in Rule 4613A that address locked or crossed quotation conditions in the ADF prior to the market opening will remain. Rule 4613A also is being modified to clarify the application of the rule in a Regulation NMS environment.

3. Conforming Changes to Reflect New Numbering of SEC Rules in Regulation NMS

NASD also is adopting conforming changes to certain NASD rules to reflect the new numbering of SEC rules in Regulation NMS. To simplify the structure of the rules adopted under Section 11A of the Exchange Act (NMS Rules), the Commission renumbered previously adopted NMS Rules, incorporated such rules into Regulation NMS and established a new definitional rule, Rule 600. Accordingly, NASD is updating all references to the NMS Rules to reflect the new SEC rule numbers.

4. Overview of NASD Certification Record Process

As noted above, critical to NASD's Regulation NMS compliance effort is the establishment of an enhanced Certification Record process for ADF Trading Centers.¹⁹ In light of the importance of the Certification Record process to NASD's Regulation NMS program, NASD filed with the Commission a copy of its proposed Certification Record.²⁰ Each enumerated item on the ADF Trading Center Certification Record will have to be certified to by a duly authorized representative²¹ of the ADF Trading Center at the time of initial application to become an ADF participant. Moreover, recertification of the ADF Trading Center Certification Record is required within 30 days of the end of each ADF Trading Center fiscal year.²²

a. Order Protection Rule Certification

Consistent with the Order Protection Rule, an ADF Trading Center is required to certify that it monitors in real time protected quotations, including the protected quotations of other ADF Trading Centers and SRO trading facilities. An ADF Trading Center also must certify that it has implemented a clock synchronization protocol such that the ADF Trading Center's internal clock used for Regulation NMS compliance purposes is set to Eastern Standard or Daylight Time, as appropriate, is synchronized to the NIST Atomic Clock and in no event deviates more than one second away from the NIST Atomic Clock.

As noted above, and required by the amendment to Rule 4300A(e), each ADF Trading Center also is required to certify that it will submit only "automated quotations"²³ for display on the ADF and that under no circumstances will a manual quotation be submitted (including a quotation that otherwise would be an automated quotation but for an ADF Trading Center system error, malfunction, latency, etc.). Moreover, each ADF Trading Center is required to certify that it offers immediate-or-cancel order execution functionality for execution against its protected quotations and that such functionality is offered to those required to be granted access to protected quotations. An ADF Trading Center must also certify that it will accept intermarket sweep orders and execute them in conformity with Regulation NMS. Each ADF Trading Center also is required to certify that its order response time will at least meet the response time required for its quotations to qualify as automated quotations under Regulation NMS. In addition, an ADF Trading Center must, among other things, certify that it will immediately transmit to NASD any notifications it receives from another trading center that has invoked the "Self-Help Exception" to the Order Protection Rule, or any notifications that it sends to another trading center that the ADF Trading Center has invoked the "Self-Help Exception" to the Order Protection Rule.²⁴

b. Access Rule Certifications

NASD is amending its ADF Trading Center Certification Record process to ensure compliance with the Access Rule. In addition to access and order reporting requirements expressly set forth in Rule 4300A, many of the certifications seek to further ensure that each ADF Trading Center will "provide a level and cost of access" to quotations displayed through the ADF "that is substantially equivalent to the level and cost of access to quotations displayed by SRO trading facilities."²⁵ Each ADF Trading Center will be required to certify that it offers fair and non-discriminatory access. Moreover, each ADF Trading Center is required to provide documentation demonstrating that it is complying with these requirements. Further, each ADF Trading Center is required to certify its acknowledgment that, to the extent that NASD deems an ADF Trading Center not to be granting the requisite level and cost of access, an ADF Trading Center will defray the connectivity costs of those persons entitled to access the ADF Trading Center.

In addition, each ADF Trading Center is required to certify that, if it charges a fee in excess of the fee cap for accessing orders other than protected quotations, it will provide functionality that prevents market participants that route orders for interaction only with protected quotes from inadvertently accessing a non-protected quotation and being charged a fee in excess of the fee cap. An ADF Trading Center also must acknowledge through the Certification Record process that NASD will not permit an ADF Trading Center's quotations to be displayed through the ADF, unless NASD determined that public notice has been provided of the ADF Trading Center's intention to display quotations through the ADF at least 60 days in advance of such activity and, at least initially, in conformity with the standard set forth by the Commission in its order extending certain Regulation NMS compliance dates.²⁶ With regard to an ADF Trading Center that displays quotations in the ADF prior to the implementation of Regulation NMS and seeks to continue uninterrupted quoting on the ADF after Regulation NMS implementation, such ADF Trading Center also must comply with this 60-day public notice period in advance of Regulation NMS implementation.

NASD requires that such advance public notice be given through reasonable means (e.g., through press releases, the NASD Web site and the ADF Trading Center's Web site). Further, each ADF Trading Center is required to certify as part of the pre-quotation notice period that it had made publicly available relevant connectivity and access technical specifications, including: (1) technical interface specifications (e.g., compatible system protocols, etc.); (2) testing schedules; (3) connectivity providers (e.g., extranet providers and direct market access firms) through which the ADF Trading Center's quotations may be accessed; and (4) all relevant subscriber and non-subscriber fees, access fees, port fees, connectivity fees and rebates.

Extend ADF Quoting and Trade Reporting Functionality to All NMS Stocks

NASD is amending rules that govern quoting, trade reporting and clearing applicable to the ADF and extending this functionality to all NMS stocks, as defined in SEC Rule 600(b)(47). Currently, the ADF accommodates the quoting, trade reporting and facilitation of clearing of only NASDAQ securities, but this rule amendment extends such rules and functionality to stocks listed on NYSE, Amex and certain other exchanges. Specifically, NASD is amending its rule to change the definition of "ADF-eligible security" to include all NMS stocks, as defined in SEC Rule 600(b)(47). In addition, NASD is amending ADF rules to adopt uniform rules governing quoting, trade reporting and comparison of NASDAQ, NYSE, Amex and certain other regionally listed securities. Since NASD is incorporating the requirements to quote and trade-report for all NMS stocks directly into the ADF rules, NASD no longer needs a separate set of rules (currently found in the Rule 6300 and 6400 Series) governing the quoting and trade reporting of NYSE, Amex and certain other regionally listed securities and is deleting these rule series.²⁷

Further, in conformity with the new standards articulated in Regulation NMS, NASD does not intend to be a participant of the Intermarket Trading System Plan (ITS Plan) or the new National Market System Linkage Plan (NMS Linkage Plan). Instead, ADF quotes in all NMS stocks will be accessible through private-connectivity providers in accordance with the quote and order access requirements set forth in Rule 4300A. This requires, among other things, that each ADF Trading Center provide direct electronic access to other ADF market participants and direct or indirect electronic access to all other registered broker-dealers seeking such access. Accordingly, because NASD does not intend to participate in the ITS Plan or the new NMS Linkage Plan, the Rule 5200 Series (containing ITS Rules) also is being deleted in its entirety.²⁸

Reorganize ADF Trade Reporting Rules to Enhance Clarity of the Rules

NASD is amending the ADF trade reporting rules to enhance their clarity. Specifically, NASD is amending Rule 4630A to clarify that a transaction executed otherwise than on an exchange would have to be reported to TRACS, in accordance with Rule 4632A or another pertinent NASD rule, unless it were reported to another facility designated by the Commission as being authorized to accept trade reports for trades executed otherwise than on an exchange.²⁹ In addition, NASD is amending Rule 4632A to reorganize the ADF trade reporting rules and to require members to report execution time in hours, minutes and seconds based on Eastern Time in military format, unless another provision of NASD rules requires that a different time be included on the report.³⁰ In general, NASD is incorporating in Rule 4632A(a) the same requirements that were previously found in Rule 5430(a), with certain technical and clarifying changes.

NASD also is amending Rule 4632A(b) to set forth which party is responsible for reporting transactions to NASD. These rules are simplified to delineate reporting responsibility between registered reporting members, non-registered reporting members, and customers or non-members. In general, Rule 4632A(b) requires the following: (1) in transactions between two registered reporting members, the sell side is required to report the trade; (2) in transactions between a registered reporting member and non-registered reporting member, the registered reporting member is required to report the trade; (3) in transactions between two non-registered reporting members, the sell side is required to report the trade; (4) in transactions between a member and a customer or non-member, the member is required to report the trade.³¹

NASD also is amending Rule 4632A(f). Currently, Rule 4632A(f) allows for the aggregation of transaction reports under certain circumstances. NASD is amending Rule 4632A(f) to expressly prohibit aggregation of individual execution of orders in a security at the same price into a single transaction report (also referred to as "bunching"). NASD has determined that it no longer should allow members to bunch transactions for reporting purposes. By prohibiting bunching, NASD will ensure greater transparency of individual transactions. NASD also is amending Rule 4632A(l) to clarify a member's obligation under ADF rules to report cancelled trades in a timely manner. Lastly, NASD is amending the Rule 6100A Series concerning the TRACS Trade Comparison Service to use terminology consistent with the ADF rules found in the Rule 4000A Series.

Endnotes

- 1 The ADF is a quotation collection, trade comparison and trade reporting facility developed by NASD in accordance with the Commission's SuperMontage Approval Order and in conjunction with NASDAQ's registration as a national securities exchange. The ADF, which currently is operating on a pilot basis, provides ADF market participants the ability to post quotations in NASDAQ securities and provides all members that participate in the ADF the ability to view quotations and report transactions in NASDAQ securities to the exclusive Securities Information Processor (SIP) for NASDAQ-listed issues for consolidation and dissemination of data to vendors and ADF market participants.
- 2 Securities Exchange Act Release No. 54537 (September 28, 2006), 71 FR 59173 (October 6, 2006) (File No. SR-NASD-2006-91).
- 3 17 CFR 242.600 *et seq.* See also Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) ("Regulation NMS Approval Order").
- 4 A "trading center" is defined in SEC Rule 600(b)(78) as a national securities exchange or national securities association that operates an SRO trading facility, ATS, exchange market maker, OTC market maker, or any other broker or dealer that executes orders internally by trading as principal or crossing as agent. See Regulation NMS Approval Order, 70 FR at 37533. In accordance with SEC Rule 611, NASD members that meet the definition of a trading center, shall establish, maintain and enforce written policies and procedures designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks that do not fall within an exception.
- 5 In addition, Regulation NMS adopted a subpenny rule that, in general, prohibits market participants from accepting, ranking or displaying orders, quotations or indications of interest in a pricing increment smaller than a penny, except for orders, quotations or indications of interest that are priced at less than \$1.00 per share. Further, Regulation NMS adopted amendments to the market data rules to update the requirements for consolidating, distributing and displaying market information, as well as amendments to the joint industry plans for disseminating market information that modify the formulas for allocating plan revenue and broadening participation in plan governance. This *Notice* describes rule amendments that primarily address implementation of the Order Protection Rule and the Access Rule. Neither the rule filing nor this *Notice* address Regulation NMS issues related to the sub-penny rule or market data rules.
- 6 NASD also is deleting IM-4613A that bans the automated update of certain quotations through the ADF. NASD originally adopted this IM to address capacity and operation concerns, but such a prohibition is no longer necessary.
- 7 Currently, Rule 4300A(e)(4) permits only five excused system outages to be granted in a 30-day period.
- 8 See 17 CFR 242.611(b). In addition, it should be noted that the SEC also adopted two new exemptions—one for "Qualified Contingent Trades" and another for "Certain Subpenny Trade-Throughs." See Securities Exchange Act Release No. 54389 (August 31, 2006), 71 FR 52829 (September 7, 2006) and Securities Exchange Act Release No. 54678 (October 31, 2006), 71 FR 65018 (November 6, 2006). To the extent that the Commission issues future exemptions or exceptions, NASD may require that additional modifiers be appended.
- 9 However, a firm would be responsible for ensuring that the specific transaction falls expressly into the exception as set forth in SEC Rule 611. Accordingly, a firm could not rely on the identification of a transaction pursuant to NASD rules as a type of trade that is excepted from Regulation NMS without ensuring the specific trade meets all of the criteria set forth in SEC Rule 611.

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- 10 Specifically, NASD will oversee NASD ADF Trading Centers and other NASD members that meet the definition of a “trading center” set forth in 600(b)(78) to determine, among other things, if they have meet their SEC Rule 611 obligations to establish, maintain and enforce written policies and procedures designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks that do not otherwise fall within an exception.
 - 11 See Regulation NMS Approval Order, 70 FR at 37543.
 - 12 See *id.*
 - 13 NASD also is amending 4300A to add a new paragraph (g) to require each Registered Reporting ADF ECN to post at least one marketable quote/order through the ADF on each side of the market each 30 calendar days or lose its ADF certification.
 - 14 See Regulation NMS Approval Order, 70 FR at 37543 (“Under Rule 610(b)(1)...ADF participants will be required to bear the costs of the necessary connectivity to facilitate efficient access to their quotations”).
 - 15 In this regard, NASD is required to evaluate “substantially equivalent” cost of access on a per transaction basis. As the Commission noted in the Regulation NMS Approval Order, this cannot be evaluated in terms of absolute dollars. For example, in evaluating access, a \$1,000 port charge for an ECN participating in ADF that trades one million shares per day would not be substantially equivalent to a \$1,000 port charge by an SRO trading facility trading 100 million shares per day. See Regulation NMS Approval Order, 70 FR at 37543. In evaluating “substantially equivalent” cost of access, NASD will look at cost related to directly accessing SRO trading facilities generally. Specifically, NASD will look at ADF Trading Center and SRO connectivity costs such as line costs and port charges. In addition, NASD also will consider costs associated with SRO membership in evaluating “substantially equivalent” costs.
 - 16 Rule 4400A, as amended, allows any registered broker-dealer to file a direct or indirect access complaint against an ADF Trading Center with NASD to allege a denial of or limitation on access. It should be noted, however, that the filing of a frivolous direct or indirect access complaint by an NASD member could constitute a violation of Rule 2110.
 - 17 The Commission noted in the Regulation NMS Approval Order that, if an ADF participant were not complying with these access standards, NASD would have a responsibility “to stop publishing the participant’s quotations until the participant comes into compliance. See Regulation NMS Approval Order, 70 FR at 37543. Rule 4400A is being amended to expressly incorporate this authority.
 - 18 It should be noted that NASD expressly prohibits the display of manual quotations in the ADF, as specified in Rule 4300A.
 - 19 NASD is amending Rule 4200A to define the term “Certification Record.” In addition, Rule 4300A is amended to expressly require compliance with the “terms agreed to in the Certification Record.”
 - 20 The SEC approved changes to the ADF Trading Center Certification Record, which became effective upon SEC approval on September 28, 2006.
 - 21 This representative typically should be the Chief Compliance Officer or other principal with appropriate oversight responsibilities.
 - 22 Current ADF Trading Centers also are required to be re-certified prior to the implementation of Regulation NMS. Accordingly, there is no “grandfather” allowance for current ADF Trading Centers.
 - 23 See 17 CFR 242.600(b)(3).
 - 24 See Regulation NMS Approval Order for a description of the “Self-Help Exception.”
 - 25 17 CFR 242.610.

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- 26 See Securities Exchange Act Release No. 53829 (May 18, 2006), 71 FR 30038 (May 24, 2006) (requiring ADF participants to meet the new automation requirements discussed above to qualify).
- 27 While ADF rules are applied in a uniform manner to all NMS stocks to the extent possible, NMS stocks are subject to two separate transaction reporting plans. NASDAQ securities are governed by the Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation, and Dissemination of Quotation and Transaction Information for NASDAQ-Listed Securities Traded on Exchanges on an Unlisted Trading Privilege Basis (UTP Plan); and NYSE, Amex, and certain other regionally listed securities are governed by the Consolidated Quotation Plan (CQ Plan) and the Consolidated Tape Association Plan (CTA Plan).
- 28 As noted above, the changes discussed in this *Notice* (including the adoption of the rules, as amended, discussed herein and the deletion of the Rule 6300 and 6400 Series) will occur on the Regulation NMS Trading Phase Date, currently scheduled to occur on February 5, 2007.
- 29 See, e.g., Securities Exchange Act Release No. 54084 (June 30, 2006), 71 FR 38935 (July 10, 2006) (File No. SR-NASD-2005-087) (establishing, among other things, rules for the trade reporting of transactions otherwise than on an exchange through the new TRF).
- 30 As described previously in the Order Protection Rule discussion, NASD also is changing the required modifiers set forth in Rule 4632A(a) to more closely align them with Regulation NMS and has inserted a general provision that requires a member to report “[a]ny other modifier as specified by NASD or the Securities and Exchange Commission.”
- 31 Rule 4200A definitions also are amended to define “registered reporting member” and “non-registered reporting member” as used in the transaction reporting rules.

Notice to Members

NOVEMBER 2006

SUGGESTED ROUTING

Institutional Customers
Legal & Compliance
Operations
Senior Management
Clearing Firms

KEY TOPICS

Customer Account Statements
DVP/RVP (Delivery versus Payment/
Receive versus Payment)
NASD Rule 2340
NASD Rule 3110
NASD Rule 11860
SEC Rule 10b-10
SEC Rule 15c3-2
SEC Rule 17a-4

GUIDANCE

Customer Account Statements

SEC Approves Amendments to Rule 2340 to Allow
DVP/RVP Customers to Elect Not to Receive Account
Statements; **Effective Date: November 22, 2006**

Executive Summary

The Securities and Exchange Commission (SEC) has approved amendments to Rule 2340 that permit customers whose accounts are carried solely for the purpose of execution on a DVP/RVP (delivery versus payment/receive versus payment) basis to opt out of receiving customer account statements.¹

The effective date of this rule change is November 22, 2006. Included with this *Notice* is Attachment A, the text of amended Rule 2340.

Questions/Further Information

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

Background and Discussion

Rule 2340 requires any member that conducts a general securities business and also carries customer accounts or holds customer funds or securities, at least once each calendar quarter, to send an account statement to each customer whose account had a security position, money balance or account activity during the time since the last statement was sent. The account statement must contain a description of any securities positions, money balances or account activity in the account.

In a DVP/RVP arrangement, payment for securities purchased is made to the selling customer's agent and/or delivery of securities sold is made to the buying customer's agent in exchange for payment at time of settlement, usually in the form of cash.² Because transactions in DVP/RVP accounts (chiefly institutional accounts) are settled directly with the agent on a transaction-by-transaction basis, account statements sent by general securities firms to customers with DVP/RVP accounts generally do not reflect any cash balance or security position at the end of a quarter. Rather than using the information provided in quarterly statements, DVP/RVP customers generally rely on trade runs or customer confirmations issued pursuant to SEC Rule 10b-10 for transaction-related information.³

The amendments to Rule 2340 relieve members from the obligation to send quarterly statements to customers with DVP/RVP accounts if: (1) the customer's account is carried solely for the purpose of execution on a DVP/RVP basis; (2) all transactions in the account are handled on a DVP/RVP basis in conformity with Rule 11860;⁴ (3) there are no securities or cash positions in the account at the end of the quarter (other than positions of a temporary nature, such as those arising from fails to receive or deliver, errors, questioned trades, dividend or bond interest entries and other similar transactions); (4) the customer consents to the suspension of such statements in writing, and the member maintains such consents in a manner consistent with Rule 3110 and SEC Rule 17a-4;⁵ (5) the member undertakes to provide any particular statement or statements to the customer promptly upon request; and (6) the member promptly undertakes to reinstate the delivery of such statements to the customer upon request.

The amendments to Rule 2340 do not qualify or condition the obligations of a member under SEC Rule 15c3-2 concerning quarterly notices of free credit balances on statements.⁶ By requiring the customer's affirmative consent, the customer's ability to receive quarterly statements is preserved, and the member is precluded from unilaterally terminating delivery of customer statements. In addition, customers are able to promptly receive particular account statements upon request, and promptly reinstate the delivery of account statements upon request.

Endnotes

- 1 See Exchange Act Release No. 54811 (Nov. 22, 2006), 71 FR 69161 (Nov. 29, 2006) (Order Approving Proposed Rule Change; File No. SR-NASD-2006-066).

This rule change is similar to a rule change proposed by the New York Stock Exchange, Inc. (now known as New York Stock Exchange LLC). See Exchange Act Release No. 53826 (May 18, 2006), 71 FR 30211 (May 25, 2006).
- 2 For purposes of Rule 2340, a DVP/RVP account is defined in Rule 2340(b) as an arrangement whereby payment for securities purchased is made to the selling customer's agent and/or delivery of securities sold is made to the buying customer's agent in exchange for payment at time of settlement, usually in the form of cash.
- 3 See SEC Rule 10b-10 (Confirmation of Transactions) and NASD Rule 11860 (Acceptance and Settlement of COD Orders).
- 4 Prior to accepting an order in a DVP/RVP account, a member must comply with Rule 11860, which requires, among other things, that the member obtain certain information from the customer, including the name and address of the agent and the account number of the customer on file with the agent.
- 5 Under NASD Rule 3110(a), NASD members are required, among other things, to make and preserve books and records as prescribed by SEC Rule 17a-3. Rule 3110 also states that the record keeping format, medium, and retention period must comply with SEC Rule 17a-4. Rule 17a-4 specifies the manner in which broker-dealers must maintain the records created in accordance with SEC Rule 17a-3, and certain other records produced by broker-dealers, and the required retention periods for these records.
- 6 SEC Rule 15c3-2 requires broker-dealers to provide each of their customers for whom a free credit balance is carried, not less frequently than once every three months, a written statement informing the customer of the amount due to the customer, and written notice that the funds are not segregated and may be used in the broker-dealer's business operations, and that the funds are payable on the customer's demand.

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ATTACHMENT A

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2300. TRANSACTIONS WITH CUSTOMERS

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2340. Customer Account Statements

(a) General

Except as otherwise provided by paragraph (b), [E]ach general securities member shall, with a frequency of not less than once every calendar quarter, send a statement of account ("account statement") containing a description of any securities positions, money balances, or account activity to each customer whose account had a security position, money balance, or account activity during the period since the last such statement was sent to the customer.

(b) Delivery Versus Payment/Receive Versus Payment (DVP/RVP) Accounts

Quarterly account statements need not be sent to a customer pursuant to paragraph (a) of this Rule if:

- (1) the customer's account is carried solely for the purpose of execution on a DVP/RVP basis;
- (2) all transactions effected for the account are done on a DVP/RVP basis in conformity with Rule 11860;
- (3) the account does not show security or money positions at the end of the quarter (provided, however that positions of a temporary nature, such as those arising from fails to receive or deliver, errors, questioned trades, dividend or bond interest entries and other similar transactions, shall not be deemed security or money positions for the purpose of this paragraph (b));
- (4) the customer consents to the suspension of such statements in writing. The member must maintain such consents in a manner consistent with Rule 3110 and SEC Rule 17a-4;
- (5) the member undertakes to provide any particular statement or statements to the customer promptly upon request; and

(6) the member undertakes to promptly reinstate the delivery of such statements to the customer upon request.

Nothing in this Rule shall be seen to qualify or condition the obligations of a member under SEC Rule 15c3-2 concerning quarterly notices of free credit balances on statements.

[(b)] **(c)** No change in text.

[(c)] **(d) Definitions**

For purposes of this Rule, the following terms will have the stated meanings:

(1) - (5) No change in text.

(6) a "DVP/RVP account" is an arrangement whereby payment for securities purchased is made to the selling customer's agent and/or delivery of securities sold is made to the buying customer's agent in exchange for payment at time of settlement, usually in the form of cash.

[(d)] **(e) Exemptions**

Pursuant to this Rule 9600 Series, [the Association] NASD may exempt any member from the provisions of this Rule for good cause shown.

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Disciplinary and Other NASD Actions

REPORTED FOR NOVEMBER

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 October 2006.

Firms Expelled, Individuals Sanctioned

Perpetual Securities, Inc. (CRD #36841, Forest Hills, New York), Cathy Yiping Huang (CRD #2370253, Registered Principal, Holmdel, New Jersey) and Youwei Paul Xu (CRD #2370245, Registered Principal, Holmdel, New Jersey). The firm was expelled from NASD membership, and Huang and Xu were barred from association with any NASD member in any capacity. The National Adjudicatory Council (NAC) imposed the sanctions following appeal of an Office of Hearing Officers (OHO) default decision. The sanctions were based on findings that the firm conducted a securities business during a suspension for failing to pay an arbitration award. The findings stated that Huang and Xu failed in their duties as the firm's principals to ensure that the firm promptly complied with its suspension. The findings also stated that Huang failed to timely and fully respond to NASD requests for documents and information. The respondents appealed NASD's findings and sanctions to the Securities and Exchange Commission (SEC). (NASD Case #C9B20040059)

Yankee Financial Group (CRD #17966, Melville, New York) and Richard Francis Kresge (CRD #729077, Registered Principal, Bay Shore, New York). The firm was expelled from NASD membership and Kresge was barred from association with any NASD member in any capacity. The NAC also ordered the firm and Kresge to pay restitution to ten customer witnesses. The NAC imposed the sanctions following appeal of an OHO decision. The firm and Kresge were ordered to pay \$3,866,426, plus interest, and realized and/or unrealized losses in the shares of a security in restitution to public customers. The sanctions were based on findings that the firm and Kresge failed to establish a reasonable system of supervision and failed to supervise the activities of firm representatives, who engaged in fraudulent solicitations and who made unsuitable recommendations to numerous customers of the firm. In these regards, the findings stated that the firm and Kresge failed to make reasonable efforts to determine that supervisory personnel and registered representatives were qualified, failed to ensure that the supervisory system reflected the significantly increased risk profile of the firm's business, failed to distribute supervisory procedures, failed to designate an office as an

Office of Supervisory Jurisdiction (OSJ), and failed to implement heightened supervisory procedures for certain representatives. The findings also included that the firm and Kresge were personally responsible for firm representatives' violations of NASD antifraud and suitability rules. NASD found that the firm and Kresge failed to report customer complaints to NASD, and failed to register an individual as a principal and a representative with NASD.

Kresge has appealed this decision to the SEC, and the bar is in effect pending consideration of the appeal. (NASD Case #CMS20030182)

Firms and Individuals Fined

Energy Securities, Inc. (CRD #101220, East Dundee, Illinois) and Lawrence Reed Buettner (CRD #2535892, Registered Principal, Village of Lakewood, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which they were fined \$15,000, jointly and severally. The firm's exemption from the requirement to qualify and register an individual as a limited principal-financial and operations was revoked. Without admitting or denying the findings, the firm and Buettner consented to the described sanctions and to the entry of findings that the firm, acting through Buettner, used the mails or other instrumentalities of interstate commerce to effect transactions in securities when it failed to maintain the minimum required net capital. (NASD Case #20050014461-01)

First New York Securities L.L.C. (CRD #16362, New York, New York) and Michael Lawrence Friedman (CRD #214675, Registered Principal, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which they were each censured and fined \$100,000. The firm was also required to revise its written supervisory procedures regarding supervision of its trading department. Without admitting or denying the findings, the firm and Friedman consented to the described sanctions and to the entry of findings that the firm failed to detect a hedge fund manager's improper short selling. The findings stated that the firm failed to detect that it had executed short sales without making or annotating affirmative determinations that the manager and the hedge fund could borrow the securities, or otherwise provide for their delivery by the settlement date. The findings also stated that the firm

failed to report the correct symbol to the Automated Confirmation Transaction ServiceSM (ACTSSM) that indicated that securities sell transactions were short sales. The findings also included that the firm effected short sales in securities for a proprietary account and a hedge fund customer, but failed to annotate or make an affirmative determination that the firm and the hedge fund could borrow the securities, or otherwise provide for their delivery by the settlement date. NASD found that the firm's supervisory system failed to provide for adequate and reasonable supervision of the hedge fund manager or the firm's trading department. (NASD Case #20050002450-03)

Torrey Pines Securities, Inc. (CRD #17120, Del Mar, California) and Jack Clark Smith, Jr. (CRD #427869, Registered Principal, San Diego, California) submitted a Letter of Acceptance, Waiver and Consent in which they were censured and fined \$15,000, jointly and severally. Without admitting or denying the findings, the firm and Smith consented to the described sanctions and to the entry of findings that, in its membership agreement, the firm, acting through Smith, represented to NASD that it would not receive securities or customer checks payable to the firm. However, during the relevant period of time, the firm, acting through Smith, received checks payable to the firm rather than to its clearing firm. The findings stated that the firm, acting through Smith, used the instrumentalities of interstate commerce to conduct a securities business while failing to maintain the minimum required net capital. The findings also stated that the firm, acting through Smith, amended its membership agreement to prohibit its receipt of customer checks payable to the firm, but failed to enforce it and, as a result, continued to receive customer checks payable to the firm. (NASD Case #E0220050158-02)

Firms Fined

A.G. Edwards & Sons, Inc. (CRD #4, St. Louis, Missouri) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$10,000 and required to provide a report to NASD attesting that it has given notice to all customers whose relationship with the firm is still controlled by any agreement containing the attorney's fee clause at issue, by letter, that the firm will not take any action to

enforce that clause. The letter also sets forth the details of notifications to customers. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it included an attorney's fee clause—which provided that the customer would be responsible for the firm's costs and attorney's fees in the event the customer brings a claim against the firm, regardless of whether or not the customer is successful in pursuing the claim in violation of NASD rules—in its customer agreements. **(NASD Case #EAF0400790002)**

Anderson & Strudwick, Incorporated (CRD #48, Richmond, Virginia) 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 regarding SEC Rule 11Ac1-6. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to make a complete report on its routing of non-directed orders in covered securities publicly available within one month after the end of each quarter. The findings stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning SEC Rule 11Ac1-6. **(NASD Case #20050000650-01)**

AXA Advisors, LLC (CRD #6627, 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 findings, the firm consented to the described sanctions and to the entry of findings that it failed to report to the Trade Reporting and Compliance Engine (TRACE) transactions in TRACE-eligible securities executed on a business day during TRACE system hours within 45 minutes of the time of execution, and incorrectly reported purchases in TRACE-eligible securities to TRACE. The findings stated that the firm failed to preserve brokerage order memoranda containing all the information required by the applicable rules for a period of no less than three years, with the first two in an accessible place. The findings also stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning TRACE reporting. **(NASD Case #20050001784-01)**

Bulltick, LLC (CRD #104005, Mexico City, Mexico) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to enforce its anti-money laundering (AML) program in a manner reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act and the implementing regulations promulgated thereunder. The findings stated that the firm opened customer accounts that did not fully comply with the requirements of its AML program, and failed to obtain certain required information in connection with the customer accounts. **(NASD Case #E062004016101)**

Cantor Fitzgerald & Co. (CRD #134, 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 findings, the firm consented to the described sanctions and to the entry of findings that it submitted to the Order Audit Trail SystemSM (OATSSM) reports with respect to equity securities traded on the NASDAQ Stock Market that were not in the electronic form prescribed by NASD and were repairable. The findings stated that OATS rejected the reports, and notice of such rejection was made available to the firm on the OATS Web site, but the firm failed to correct or replace the reports. The findings also stated that the firm published quotations in the OTC Equity securities or directly or indirectly submitted the quotations for publication in a quotation medium, but failed to have the documentation SEC Rule 15c2-11(a) required in its records, did not have a reasonable basis under the circumstances for believing that the information was accurate in all material respects, that the sources of the information were reliable and that the quotations did not represent a customer's indication of unsolicited interest. The findings also included that the firm failed to file a Form 211 with NASD at least three business days before its quotations were published or displayed in a quotation medium. NASD found that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with SEC Rule 15c2-11 and NASD Marketplace Rule 6740. **(NASD Case #20050018123-01)**

Feldman Securities Group, L.L.C. (CRD #39385, Chicago, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$22,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it published research reports that were deficient. The findings stated that the firm's written supervisory procedures were incomplete in certain respects and that the firm did not fully implement other procedures with regard to its dissemination of research reports containing disclosure deficiencies. The findings also stated that the firm did not balance favorable discussions of securities identified in research reports with sufficient disclosures of risks associated with an investment in the securities. The findings also included that the firm did not fully ensure compliance with SEC Regulation AC, in that some research reports did not include an Analyst Certification. **(NASD Case #E8A2005007601)**

Fieldstone Services Corp. (CRD #27851, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$150,000 and required to review its systems and procedures with regards to the preservation of electronic mail communications for compliance with NASD rules and federal securities laws and regulations. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that the firm failed to maintain and preserve all of its email communications, as required. The findings stated that the firm used the instrumentalities of interstate commerce to conduct a securities business while failing to maintain its minimum required net capital. The findings also stated that the firm failed to file its annual audited report for one year in a timely manner. The findings also included that the firm failed to comply with its membership agreement, which permitted the firm to engage in transactions involving fixed-income and private placement securities by engaging in equity transactions. NASD found that the firm failed to establish, maintain and enforce written procedures to supervise the types of business in which it engaged. NASD also found that the equity trade tickets the firm executed failed to contain either an order receipt or an order entry time, and customer confirmations issued to public customers failed to indicate that transactions were riskless principal trades. **(NASD Case #E102004015503)**

Fox & Company Investments, Inc. (CRD #18517, Phoenix, Arizona) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$25,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to timely and accurately update the Uniform Termination Notice for Securities Industry Termination (Form U5) for former registered representatives for events that required regulatory disclosure. The findings stated that the firm failed to timely and accurately report municipal bond transactions to the MSRB, and erroneously made reports to the MSRB for transactions that did not actually occur. The findings also stated that the firm failed to make and keep current order tickets for municipal securities transactions. The findings also included that the firm failed to adopt and maintain written supervisory procedures reasonably designed to achieve compliance with MSRB rules. **(NASD Case #E3A20050043-02)**

Gilford Securities Incorporated (CRD #8076, New York, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$30,000 and required to revise its written supervisory procedures regarding TRACE reporting. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to report transactions in TRACE-eligible securities to TRACE, and failed to report the lower of yield to call or yield to maturity for transactions in TRACE-eligible transactions to TRACE. The findings stated that the firm, when it acted as principal for its own account, failed to provide its customers with written notification disclosing the yield at which the transactions were effected. The findings also stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning TRACE reporting. **(NASD Case #20050001803-01)**

Goldman Sachs Execution & Clearing, L.P. (CRD #3466, Jersey City, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$28,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to classify an order correctly as a market limit order, failed to report accurate order execution data and improperly published statistics for all limit order groups.

The findings stated that the firm transmitted reports to OATS that contained inaccurate, incomplete or improperly formatted data. The findings also stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning order handling under SEC Rule 605, best execution, anti-intimidation, trade reporting, sales transactions and SEC Reg. SHO, and soft dollars. **(NASD Case #20050023633-01)**

Hunter Securities Corp. (CRD #13134, Maplewood, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to report transactions in municipal securities to the MSRB within 15 minutes of the execution time. **(NASD Case #20050034103-01)**

INTL Trading, Inc. (CRD #45993, Altamonte Springs, Florida) 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 regarding compliance with SEC Rule 15c2-11 and NASD Marketplace Rule 6740. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it submitted quotations on a quotation medium and did not have the required documentation representing a customer's indication of unsolicited customer interest in its records. The findings stated that the firm failed to file a Form 211 with NASD at least three business days before the firm's quotations were published or displayed in a quotation medium. The findings also stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning SEC Rule 15c2-11 and NASD Marketplace Rule 6740. **(NASD Case #20050030714-01)**

Knight Capital Markets, LLC (CRD #38379, Purchase, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$40,000 and required to revise its written supervisory procedures regarding NASD Marketplace Rule 5220(e). Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that, as an intermarket trading system/ computer assisted execution system (ITS/CAES) market

maker, it purchased or sold ITS/CAES securities whether in a principal capacity or as an agent at a price lower than the bid or higher than the offer displayed from an ITS participant exchange or ITS/CAES market maker. The findings stated that the firm, as a registered market maker in securities, was presented orders at its published bid or offer in an amount up to its published quotation size, and failed to execute the orders upon presentment, thereby failing to honor its published quotation. The findings also stated that the firm, an ITS/CAES market maker, failed to maintain continuous two-sided quotations in the absence of the grant of an excused withdrawal or a functional excused withdrawal by NASD. The findings also included that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules. **(NASD Case #20050000863-01)**

Morgan Keegan & Company, Inc. (CRD #4161, Memphis, Tennessee) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$29,500. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to timely file amendments to Uniform Applications for Securities Industry Registration or Transfer (Forms U4), and failed to timely file Forms U5 with NASD. **(NASD Case #2005002050701)**

Morgan Keegan & Company, Inc. (CRD #4161, Memphis, Tennessee) was censured and fined \$22,300. The sanctions were based on findings that the firm sold into the OTC Bulletin Board market, shares of an unregistered security and transferred shares from a public customer's trust account into other accounts at the firm using means or instruments of transportation or communication of interstate commerce. The findings stated that the firm failed to establish that the security was exempt from SEC and NASD registration requirements. **(NASD Case #CAF040073)**

Morgan Stanley DW Inc. (CRD #7556, Purchase, New York) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$500,000 (to be paid jointly to NASD, the American Stock Exchange and the New York Stock Exchange) and required to revise its written supervisory procedures regarding short interest reporting. Without admitting or denying the findings, the firm consented to the

described sanctions and to the entry of findings that it utilized "z indicators" in its Security Master File for securities traded on multiple exchanges, but the firm's short interest reports short positions omitted securities labeled with the "z indicator." The findings stated that the firm failed to report its short interest positions in preferred and affiliates' securities. The findings also stated that the firm failed to reasonably and properly supervise its process for reporting short interest to NASD, in that it failed to detect inaccuracies associated with its short interest reports and failed to have an adequate system of follow up and review for compliance with self-regulatory organization rules with respect to short interest reporting. The findings also included that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning short interest reporting. (NASD Case #20050024147-01)

Oddo Securities Corporation (CRD #45104, 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 findings, the firm consented to the described sanctions and to the entry of findings that it failed to implement an AML program that was reasonably designed to achieve and monitor compliance with the requirements of the Bank Secrecy Act and the implementing regulations promulgated thereunder by the Department of Treasury. (NASD Case #E102005032601)

Pond Equities (CRD #30934, Brooklyn, 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 findings, the firm consented to the described sanctions and to the entry of findings that it conducted a securities business while failing to maintain the minimum required net capital. The findings stated that the firm failed to report the correct symbol indicating the firm's capacity as either principal or agent to ACT in numerous transactions; it reported transactions without the .T modifier, used the incorrect capacity and failed to report transactions in debt securities reportable under TRACE. The findings also stated that the firm failed to timely and properly report OTC equity security transactions through ACT, and failed to report transactions with the correct order identifier when reporting transactions in OTC equity transactions to ACT, that were executed outside normal

market hours. The findings also included that the firm failed to report transactions to ACT for transactions in eligible securities listed on a national exchange, which were traded otherwise than on a national securities exchange, failed to report transactions to ACT with the correct order identifier and failed to timely report transactions to ACT for transactions in eligible securities listed on a national exchange that were traded otherwise than on a national securities exchange. NASD found that the firm failed to timely and properly report transactions in NASDAQ National Market and NASDAQ SmallCap Market securities through ACT, failed to record the reported price or the difference between the reported price and the price to the customer on its order confirmations, and the order confirmations failed to disclose that the firm acted as a market maker in that security. NASD also found that the firm's two inter-dealer transactions were not reported to the MSRB. (NASD Case #ELI2004014601)

Reid & Rudiger LLC (CRD #47263, New York, New York) submitted an Offer of Settlement 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 properly time stamp order tickets, in that the tickets did not contain a time stamp indicating the time the orders were received, and failed to show the time in seconds on order entries. The findings stated that the firm failed to maintain AML procedures that were approved in writing by senior management and did not provide for prompt notification to NASD regarding designation and identification of individuals responsible for monitoring the AML program. The findings also stated that the firm's Customer Identification Program failed to address verification procedures. (NASD Case #E1020040343-01)

Seaboard Securities, Inc. (CRD #755, Florham Park, New Jersey) 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 regarding SEC Rule 606, best execution, SEC Rule 605, trade reporting, affirmative determination, Chinese walls, and books and records. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it failed to accept or decline transactions in eligible securities in the NASDAQ Market Center within 20 minutes after execution and failed to report the correct

symbol indicating whether the firm executed transactions in eligible securities in a principal or agency capacity. The findings stated that the firm failed to correctly report riskless principal transactions in last sale reports of transactions in OTC equity securities through the NASDAQ Market Center. The findings also stated that the firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning SEC Rule 606, best execution, SEC Rule 605, trade reporting, affirmative determination, Chinese walls, and books and records. **(NASD Case #20050002610-01)**

SF Investments, Inc. (CRD #6564, Highland Park, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$10,000. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it made untimely TRACE reports, reported the incorrect volume and reported transactions it was not required to report. The findings stated that the firm reported the time of municipal securities transactions inaccurately and late, reported transactions it was not required to report, reported the volume inaccurately in a transaction and failed to report transactions. **(NASD Case #E8A2005018701)**

Sharebuilder Securities Corporation (CRD #45744, Bellevue, Washington) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$140,000 and required to file all advertisements used on the firm's Web site or on the Internet with NASD at least 10 days prior to their first use for one year. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that it committed several violations of NASD's advertising rules by means of various false and misleading statements regarding its services, including predictions of performance, incomplete and unbalanced comparisons with its Web site and Internet advertising. The findings stated that these misleading advertisements were available for widespread use by the investing public, not only for those who were the firm's customers. The findings also stated that the firm failed to file Exchange Traded Funds (EFT) related communications with NASD as it was required to do. **(NASD Case# 2006003887001)**

Tower Square Securities, Inc. (CRD #833, Hartford, Connecticut) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured, fined \$85,000 and required to review its written supervisory procedures and establish a supervisory system reasonably designed to achieve compliance with laws, regulations and rules concerning pre-registration Web CRD searches. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that its supervisory system and procedures were not reasonably designed to ensure that the firm obtained and/or retained required written consent for pre-registration searches on Web CRD. The findings stated that, as the result of supervisory deficiencies, the firm failed to obtain and/or retain the required written consent in connection with its pre-registration searches of individuals, many of whom were not seeking employment with the firm or were seeking employment with an affiliated broker-dealer and not the firm. With respect to the latter searches, the individuals seeking employment with an affiliated broker-dealer had consented to a pre-registration search by the affiliated broker-dealer, but not by Tower Square. The findings also stated that the firm failed to implement a written AML program reasonably designed to achieve compliance with the requirements the Bank Secrecy Act and the regulations promulgated thereunder imposed. **(NASD Case #E112005002601)**

Wells Fargo Brokerage Services, L.L.C. (CRD #16100, Minneapolis, Minnesota) submitted a Letter of Acceptance, Waiver and Consent in which the firm was censured and fined \$12,500. Without admitting or denying the findings, the firm consented to the described sanctions and to the entry of findings that when it reported corporate debt transactions to TRACE, the firm, which was acting in a principal capacity, incorrectly reported a commission charge. The firm's supervisory system did not provide for supervision reasonably designed to achieve compliance with applicable securities laws, regulations and NASD rules concerning accurate TRACE reporting. **(NASD Case #20050001807-01)**

Individuals Barred or Suspended

John Ivey Amon, Jr. (CRD #4489, Registered Representative, Goldsboro, North Carolina) 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 four months. The fine must be paid before Amon reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Amon consented to the described sanctions and to the entry of findings that he re-allocated a public customer's sub-account holdings for a variable annuity totaling \$13,000 from a guaranteed fixed rate to equity mutual funds without the customer's knowledge or authorization. The findings stated that Amon agreed to reimburse the customer for his incurred losses as a result of the unauthorized transactions, wrote a check for \$577.56, and then had these funds deposited directly into the customer's annuity without disclosing the settlement to his member firm.

The suspension in any capacity is effective from October 16, 2006 through February 15, 2007. (NASD Case #2005002553601)

Maxi Joel Arias (CRD #4556162, Registered Representative, Bronx, 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 findings, Arias consented to the described sanction and to the entry of findings that he falsified customer signatures on insurance applications. The findings stated that Arias failed to respond to NASD requests for information. (NASD Case #2006004268401)

Robert Francis Arimenta, Sr. (CRD #7103, Registered Supervisor, Princeton, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$20,000 and suspended from association with any NASD member in any principal capacity for three months. The fine must be paid before Arimenta reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Arimenta consented to the described sanctions and to the entry of findings that his member firm, acting through Arimenta, did not have an

adequate supervisory system and procedures that were reasonably designed to oversee the trading activities of its registered representatives at the firm's Financial Advisory Center (FAC), referred to within the firm as Investment Service Advisors (ISAs). The findings stated that the firm, acting through Arimenta, failed to establish and maintain a supervisory system and written procedures reasonably designed to achieve compliance with NASD Rule 2830, in that the FAC conducted sales contests that violated the non-cash compensation rule. The findings also stated that the firm, acting through Arimenta, allowed "lead advisors" to exercise certain direct supervisory responsibility over ISAs when the majority of the lead advisors were not properly registered as principals and lacked sufficient qualifications to supervise ISAs on their teams.

The suspension in any principal capacity will be in effect from October 2, 2006 through January 1, 2007. (NASD Case #E9B2003042105)

Robert Lee Banks (CRD #4909350, Associated Person, Zuni, Virginia) was barred from association with any NASD member in any capacity. The sanction was based on findings that Banks failed to respond to NASD requests for information. The findings stated that Banks willfully failed to disclose material information on his Form U4. (NASD Case #2005000524901)

Steven Anthony Bencivenga, Jr. (CRD #3000161, Registered Representative, Brooklyn, New York) submitted an Offer of Settlement in which he was fined \$15,000, ordered to pay \$553 in restitution to public customers and suspended from association with any NASD member in any capacity for five months. Without admitting or denying the allegations, Bencivenga consented to the described sanctions and to the entry of findings that he effected securities transactions in public customers' account without their prior knowledge, authorization or consent, and without having reasonable grounds for believing that the transactions were suitable for the customers based upon their financial situations, investment objectives and financial needs. The findings stated that Bencivenga failed to make reasonable efforts to obtain information from customers concerning their financial status, tax status and other information used or considered to be reasonable in making recommendations to them. The findings also included that Bencivenga caused his member firm to make unlawful credit extensions in the

public customers' account and engaged in "free-riding" transactions in their account.

The suspension in any capacity will be in effect from October 16, 2006 through March 15, 2007. (NASD Case #E1020031192-01)

James William Brophy (CRD #1144654, Registered Representative, Winston Salem, North Carolina) submitted a Letter of Acceptance, Waiver and Consent in which he was suspended from association with any NASD member in any capacity for 15 business days. In light of Brophy's financial status, no monetary sanction has been imposed. Without admitting or denying the findings, Brophy consented to the described sanction and to the entry of findings that he made a recommendation to a public customer without having reasonable grounds for believing that the recommendation was suitable for the customer based on her investment objective of liquidity.

The suspension in any capacity was in effect from October 16, 2006 through November 3, 2006. (NASD Case #2005002714501)

Tyrone Vandelle Burroughs (CRD #2048487, Registered Representative, Hampton, Georgia) was barred from association with any NASD member in any capacity. The sanction was based on the findings that Burroughs engaged in outside business activities for compensation without providing prompt written notification to his member firm. The findings stated that Burroughs gave false written statements to NASD. (NASD Case# E072004082401)

John Michael Carson (CRD #41916, Registered Representative, Fayetteville, Georgia) was barred from association with any NASD member in any capacity. The sanction was based on findings that Carson failed to appear for an NASD on-the-record interview. (NASD Case # E072004075201)

Timothy George Clouse (CRD #1647709, Registered Principal, Lake Orion, 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 findings, Clouse consented to the described sanction and to the entry of findings that he partially completed and signed forms for public customers to purchase securities, and altered information or inserted new information related

to sales/surrender charges without informing the customers he was altering the documents. (NASD Case #2004064801)

David Joseph Cottam (CRD #2716994, Registered Representative, Kinnelon, New Jersey) submitted an Offer of Settlement in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 18 months. The fine must be paid before Cottam reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Cottam consented to the described sanctions and to the entry of findings that he improperly obtained Contingent Deferred Sales Charge (CDSC) waivers for public customers in connection with mutual fund redemptions by falsely representing, on his member firm's electronic order entry system, that the customers were disabled, when in fact, they were not. The findings stated that as a result, several mutual funds companies were deprived of fees to which they were otherwise entitled. The findings also stated that Cottam's actions caused his member firm's books and records relating to redemptions to contain false and misleading information regarding the disability status of the customers and their entitlement to a CDSC waiver.

The suspension in any capacity is in effect from October 16, 2006 through April 15, 2008. (NASD Case #E9B2003026301)

Claude Eugene Crump (CRD #1619470, Registered Principal, Buckeye, Arizona) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$8,000 and suspended from association with any NASD member in any capacity for 30 business days. The fine must be paid before Crump reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Crump consented to the described sanctions and to the entry of findings that he engaged in an outside business activity from which he received compensation and failed to provide prompt written notice to his member firm. The findings stated that Crump disseminated sales literature to public customers without his member firm's written approval.

The suspension in any capacity is in effect from October 16, 2006 through November 27, 2006. (NASD Case #2005003350801)

Timothy John Dabulis (CRD #2302842, Registered Representative, Pompano Beach, Florida) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the findings, Dabulis consented to the described sanctions and to the entry of findings that he effected unauthorized transactions totaling \$5,019.88 in a public customer's account.

The suspension in any capacity was in effect from October 16, 2006 through October 27, 2006. **(NASD Case #2005002672501)**

Timothy James Daly (CRD #1460203, Registered Principal, Weston, Connecticut) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$15,000 and barred from association with any NASD member in a principal capacity. The fine must be paid before Daly reassociates with any NASD member, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Daly consented to the described sanctions and to the entry of findings that he failed to establish and maintain a supervisory system and written procedures reasonably designed to supervise his firm's registered representatives' and associated persons' activities to achieve compliance with applicable securities laws, regulations and NASD rules. The findings stated that Daly, acting on his member firm's behalf, failed to conduct internal inspections of its offices of supervisory jurisdiction in accordance with the requirements of NASD Rule 3010(c). The findings also stated that Daly, acting on his member firm's behalf, failed to establish procedures for the review of transactions and its registered representatives' correspondence with the public. The findings also included that the firm, acting through Daly, operated its business without a limited principal/financial and operations principal (FINOP). **(NASD Case #E112005009201)**

Robert Thomas Davis III (CRD #1806076, Registered Representative, Sumter, South Carolina) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in any capacity and ordered to pay a public customer \$104,000, plus interest, in restitution. The restitution must be paid before Davis reassociates with any NASD member, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Davis consented to the described sanctions

and to the entry of findings that he withdrew \$104,000 from a public customer's annuity contract without her knowledge or approval, and converted the funds for his own personal benefit. The findings stated that Davis entered into a settlement agreement with the customer in which he promised to repay the \$104,000, did not notify his member firm that he entered into such agreement and did not repay the customer as promised. **(NASD Case #2005002609101)**

Carmine DePalma (CRD #1838261, Registered Principal, Mt. Kisco, New York) was barred from association with any NASD member in any capacity. The sanction was based on findings that DePalma made an unsuitable recommendation to a public customer in light of the customer's financial status, investment objective and risk tolerance. The findings stated that DePalma engaged in private securities transactions without providing prior written notice to, and obtaining written authorization from, his member firm. The findings also stated that DePalma participated in outside business activities from which he received compensation and failed to provide prompt written notice to his member firm. The findings also included that DePalma falsified records in that he provided confirmations of the customer's investments that bore the corporate insignia of an entity that had no connection to the customer's transactions. **(NASD Case #ELI20040233-01)**

Jean B. Dorsainvil (CRD #4805617, Registered Representative, Bronx, 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 findings, Dorsainvil consented to the described sanction and to the entry of findings that he caused checks totaling \$17,400 to be issued from public customers' annuity accounts without the customers' knowledge or consent by forging their signatures on annuity withdrawal forms, depositing the funds into his own bank accounts and subsequently withdrawing the funds for his own use. The findings stated that Dorsainvil failed to respond to NASD requests for information. **(NASD Case #2006004899101)**

John Alfred Elam, Jr. (CRD #1334930, Registered Principal, Virginia Beach, Virginia) was barred from association with any NASD member in any capacity. The sanction was based on findings that Elam failed to respond to NASD requests for information and documents. The findings stated that Elam willfully failed

to amend his Form U4 to disclose material information. (NASD Case #2005002600501)

Robert Eugene Elkins (CRD #2618105, Registered Representative, Redford, Michigan) was fined \$5,000 and suspended from association with any NASD member in any capacity for one year. The sanctions were based on findings that Elkins sold, or caused to be sold, an increased number of shares of a mutual fund in a public customer's account without the customer's knowledge or consent.

The suspension in any capacity is in effect from September 18, 2006 through September 17, 2007. (NASD Case #E8A2003080701)

Phillip Lee Elliott (CRD #1410115, Registered Principal, Lexington, Kentucky) 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 Elliott reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Elliott consented to the described sanctions and to the entry of findings that he effected, or caused to be effected, bond transactions in a public customer's account on a discretionary basis without the customer's prior written authorization to exercise discretion, and without his member firm's written acceptance of the account as discretionary.

The suspension in any capacity was in effect from October 16, 2006 through October 27, 2006. (NASD Case #2005002250601)

Roger Ernest Frank (CRD #1620117, Registered Representative, Riverside, Connecticut) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$17,500 and suspended from association with any NASD member in any capacity for 15 business days. Without admitting or denying the findings, Frank consented to the described sanctions and to the entry of findings that he traded securities through an account maintained at another member firm without providing notice to his member firm or notice of his association with the firm that maintained that account. The findings stated that Frank engaged in private securities transactions without providing prior written notice to his member firm.

The suspension in any capacity is in effect from November 6, 2006 through November 27, 2006. (NASD Case #E1020041096-01)

John Joseph Fratello (CRD #213241, Registered Representative, Brooklyn, 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 in any capacity for three months. The fine must be paid before Fratello reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Fratello consented to the described sanctions and to the entry of findings that he failed to respond to NASD requests for information in a timely manner.

The suspension in any capacity is in effect from November 6, 2006 through February 5, 2007. (NASD Case #2005000731601)

John Sherwood Gee Jr. (CRD #873896, Registered Principal, Titusville, New Jersey) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$25,000 and suspended from association with any NASD member in any principal capacity for four months. The fine must be paid before Gee reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Gee consented to the described sanctions and to the entry of findings that his member firm, acting through Gee, did not have an adequate supervisory system and procedures reasonably designed to oversee the trading activities of its registered representatives at the firm's FAC, referred to within the firm as ISAs. The findings also stated that the firm, acting through Gee, failed to establish and maintain a supervisory system and written procedures reasonably designed to achieve compliance with NASD Rule 2830.

The suspension in any principal capacity is in effect from October 2, 2006 through February 1, 2007. (NASD Case #E9B2003042106)

Kimberly Pine Hardaker (CRD #1816093, Registered Principal, Laguna Niguel, California) 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 findings, Hardaker consented to the described sanction and to

the entry of findings that she acted as a broker-dealer without being registered with the SEC. The findings stated that Hardaker participated in a private securities transaction, for compensation, without providing prior written notice to, and receiving prior written approval from, her member firm. The findings also stated that Hardaker received \$543,630 from public customers for the purchase of securities and commingled the monies with unrelated funds subjecting the customer funds to a risk of loss. The findings also included that Hardaker created and mailed confirmation statements to public customers purporting to evidence the securities purchases. NASD found that on the confirmation statements Hardaker provided to the customers, she failed to disclose that the price of the shares included a one cent per share markup. **(NASD Case #20050002046-01)**

Wayne Jason Herman (CRD #4525495, Registered Representative, Hewlett, New York) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 60 days. The fine must be paid before Herman reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Herman consented to the described sanctions and to the entry of findings that he failed to amend his Form U4 to disclose material information.

The suspension in any capacity is in effect from October 2, 2006 through November 30, 2006. **(NASD Case #2006004713801)**

Timothy Martin Hughes (CRD #2161692, Registered Representative, Franklin Square, 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 findings, Hughes 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 #20050012141-04)**

Linda Carol Hopkins (CRD #1872850, Registered Principal, Aurora, Ohio) submitted a Letter of Acceptance, Waiver and Consent in which she was fined \$10,000 and suspended from association with any NASD member in any capacity for one year. The fine must be paid before Hopkins reassociates with

any NASD member following the suspension, or before she requests relief from any statutory disqualification. Without admitting or denying the findings, Hopkins consented to the described sanctions and to the entry of findings that she failed to respond to NASD requests for information in a timely manner.

The suspension in any capacity is in effect from October 16, 2006 through October 15, 2007. **(NASD Case #E8A2004026302)**

Stacie Anne Hopkins (ICRD #1288359, Registered Principal, Queensburg, New York) 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 findings, Hopkins consented to the described sanction and to the entry of findings that she failed to appear for an NASD on-the-record interview. **(NASD Case #20050005515-02)**

Ryan Michael Jindra (CRD #4085610, Registered Principal, Omaha, Nebraska) 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 Jindra reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Jindra consented to the described sanctions and to the entry of findings that he participated in outside business activities, for compensation, without providing his member firm with prompt written notice.

The suspension in any capacity is in effect from October 16, 2006 through November 27, 2006. **(NASD Case #20060045274-01)**

Marvin Ray Koerselman (CRD #1195716, Registered Representative, Westminster, Colorado) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for three months. The fine must be paid before Koerselman reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Koerselman consented to the described sanctions and to the entry of findings that he engaged in outside business activities and failed to provide his

member firm with prompt written notice. The findings stated that Koerselman completed and submitted questionnaires to his member firm wherein he falsely indicated that he was complying with the firm's requirement that he not accept customer checks made payable to him.

The suspension in any capacity is in effect from October 16, 2006 through January 15, 2007. (NASD Case #2005001737201)

William Michael Kuether (CRD #4897471, Associated Person, Clear Lake, 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 findings, Kuether consented to the described sanction and to the entry of findings that he willfully failed to disclose a material fact on his Form U4. The findings stated that Kuether failed to respond truthfully to an NASD request for information and failed to respond to subsequent requests for information. (NASD Case #20050013765-01)

Gary Lynn Lancaster (CRD #2730640, Registered Representative, Vancouver, 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 findings, Lancaster consented to the described sanction and to the entry of findings that he participated in private securities transactions and failed to provide his member firm with written notice. (NASD Case #20050034080-01)

David John Leyshon (CRD #1146050, Registered Representative, Peoria, Arizona) was barred from association with any NASD member in any capacity. The sanction was based on findings that Leyshon recommended and executed securities transactions in a public customer's account without having a reasonable basis for believing that his recommendations to the customer were suitable based on the account's turnover rate, short-term nature of the trading and the cost-to-equity ratio. The findings stated that Leyshon recommended and effected an excessive number of trades in the customer's account in complete disregard for her interests. The findings also stated that Leyshon executed securities transactions in the customer's account without the customer's prior authorization. The findings also included that Leyshon intentionally submitted false customer information to his member

firm; this caused its records to be inaccurate and misleading. NASD found that Leyshon failed to respond to NASD requests for information. (NASD Case #E3A2004035601)

Melissa A. Licht (CRD #4470617, Registered Representative, Pittsburgh, Pennsylvania) submitted an Offer of Settlement in which she was barred from association with any NASD member in any capacity. Without admitting or denying the allegations, Licht consented to the described sanction and to the entry of findings that she forged signatures on blank checks her supervisor owned that pertained to an account at the firm, made the checks payable to herself in the total amount of \$8,500, endorsed the checks and deposited them into her personal account without her supervisor's authorization or consent. The findings stated that Licht failed to respond to NASD requests for information. (NASD Case #2005002708301)

Peter J. Maldjian (CRD #4471819, Registered Principal, Brielle, New Jersey) submitted an Offer of Settlement 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, Maldjian consented to the described sanctions and to the entry of findings that he created and submitted a fictitious certificate of formation for a limited liability company to his member firm in attempt to open a brokerage account at his member firm, used the business filing number from another *bona-fide* limited liability company and replicated the New Jersey State Treasurer "filed" stamp. The findings stated that the false certificate of formation gave the impression that the firm was a *bona-fide* New Jersey established limited liability company, when in fact it was not.

The suspension in any capacity is in effect from October 16, 2006 through January 15, 2007. (NASD Case #E9B2004028401)

William Andrew Malloy (CRD #1492864, Registered Principal, Matthews, North Carolina) submitted a Letter of Acceptance, Waiver and Consent in which he was barred from association with any NASD member in a principal or supervisory capacity. Without admitting or denying the findings, Malloy consented to the described sanction and to the entry of findings that he failed to perform branch audits and failed to conduct regular

compliance reviews of trading activity in customer accounts as his firm's written supervisory procedures required. (NASD Case #20050000286-02)

Marqusia Shanti Melton (CRD #4891774, Associated Person, Milwaukee, Wisconsin) was barred from association with any NASD member in any capacity. The sanction was based on findings that Melton failed to respond to NASD requests for information. The findings stated that Melton failed to disclose material information on her Form U4. (NASD Case #2005000725701)

Corey Dwayne Minor (CRD #3136902, Registered Principal, DeSoto, 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 findings, Minor consented to the described sanction and to the entry of findings that he misused public customer funds by depositing \$18,800 designated for the purchase of corporate bonds into an account he controlled, then sent, or caused to be sent, account statements to customers falsely showing that he had purchased the bonds. The findings stated that Minor failed to timely and completely respond to NASD requests for documents. (NASD Case #2005002299901)

Mary Ann Naventi (CRD #2656084, Registered Principal, New Milford, Connecticut) 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 findings, Naventi consented to the described sanction and to the entry of findings that she falsely notarized the signatures of persons on deeds and a mortgage document without having actually witnessed the signatures. (NASD Case #2006004215401)

Hung The Nguyen (CRD #2532462, Registered Representative, Orlando, Florida) 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 Nguyen reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. The sanctions were based on findings that Nguyen failed to disclose his activities relating to an outside securities account to his member firm.

The suspension in any capacity was effective from October 2, 2006 through November 10, 2006. (NASD Case #E072004087801)

Corey C. Ohle (CRD #4937958, Registered Representative, River Ridge, Louisiana) 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 findings, Ohle consented to the described sanction and to the entry of findings that he withdrew \$2,000 from a public customer's savings account without the customer's knowledge or authorization and converted the funds to his own use and benefit. The findings stated that Ohle failed to respond to NASD requests for information. (NASD Case #2006004899801)

David John Palen (CRD #2321162, Registered Representative, Scottsdale, Arizona) was barred from association with any NASD member in any capacity. The sanction was based on findings that Palen withdrew approximately \$203,000 from public customer accounts to pay for financial planning fees that the customers had not authorized or approved. The complaint alleges that Palen signed a public customer's name to an advisory service agreement without the customer's authorization or consent and submitted it to his member firm. The complaint also alleges that Palen failed to appear for an NASD on-the-record interview. (NASD Case #E3A2004036501)

Samuel Conant Parks (CRD #602872, Registered Representative, Kingston, 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 findings, Parks consented to the described sanction and to the entry of findings that he, intentionally or recklessly, failed to disclose that he had received compensation from the issuer for his recommendations and sales of a stock to public customers. The findings stated that Parks failed to disclose conflict of interest and compensation to customers in that he knew, or had reason to know, that the agreement to compensate him for the sale of the stock and subsequent payments to him created an actual material conflict of interest at the time of he published research reports regarding the stock. The findings also stated that Parks participated in private securities transactions, for compensation, without

providing prior notice to, and receiving approval from, his member firm. The findings also included that Parks opened an account with another firm without providing prior notification to his member firm or of his association with the other member firm, and falsely stated that no NASD registered person had an interest in the account on a new account signature card. **(NASD Case #E3B2004021902)**

James Francis Queeny (CRD #1088832, Registered Representative, Duxbury, Massachusetts) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$56,000, of which \$51,000 is disgorgement of commission, and suspended from association with any NASD member in any capacity for 30 days. Without admitting or denying the findings, Queeny consented to the described sanctions and to the entry of findings that he participated in private securities transaction without his member firm's approval.

The suspension in any capacity was in effect from October 16, 2006 through November 14, 2006. **(NASD Case #E112004031101)**

David G. Rincon (CRD #4598476, Registered Representative, Westbury, 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 in any capacity for 60 days. The fine must be paid before Rincon reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Rincon consented to the described sanctions and to the entry of findings that he provided a public customer with a document that contained misleading statements. The findings stated that Rincon failed to respond to the customer's request to enter stop loss orders for positions in the customer's account.

The suspension in any capacity will be in effect from October 2, 2006 through November 30, 2006. **(NASD Case #20050010905-01)**

Richard Lewis Rosen (CRD #1643922, Registered Principal, New York, New York) was barred from association with any NASD member in any capacity. The sanction was based on findings that a member firm, acting through Rosen, served as a broker for

transactions that involved unregistered securities for which Rosen received commissions. The findings stated that a member firm, acting through Rosen, violated its membership agreement with NASD and effected material changes in his member firm's business operations without filing an application for approval with NASD. The findings also stated that Rosen failed to complete the regulatory element of NASD's Continuing Education requirement, which caused his registration to be inactive while he continued to effect securities transactions and serve as a president of the firm. The findings also included that the firm, acting through Rosen, effected securities transactions while failing to meet its minimum net capital requirement. NASD found that the firm, acting through Rosen, did not have an adequate system in place for the retention of electronic mail, failed to designate a FINOP for more than a year, failed to create and maintain a general ledger, and to create records that reflected the firm's assets and liabilities, income and expenses and capital accounts. **(NASD Case #E102002179201)**

Robert Michael Ryerson (CRD #1224662, Registered Principal, Freehold, New Jersey) was fined \$230,000, suspended from association with any NASD member in any capacity for two years and ordered to re-qualify in all capacities for engaging in private securities transactions. Ryerson was also fined \$5,000 and suspended from association with any NASD member in any capacity for 15 business days for payment of commissions to an unregistered entity. The suspensions shall run concurrently. The NAC imposed the sanctions following appeal of an OHO decision. The sanctions were based on findings that Ryerson engaged in private securities transactions, for compensation, without providing prior written notice to, and receiving prior written approval from, his member firm. The findings also stated that Ryerson paid \$100,000 in commissions to a non-member firm in connection with variable annuity referrals that he had received. Finally, the findings stated that Ryerson failed to fully and promptly provide on-the-record testimony NASD requested. No additional sanction, however, was imposed for Ryerson's failure to provide required testimony.

The suspension in any capacity is in effect from October 2, 2006 through October 1, 2008. **(NASD Case #C9B20040033)**

Arun Kumar Salwan (CRD #4288865, Registered Representative, Schaumburg, Illinois) 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 Salwan reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Salwan consented to the described sanctions and to the entry of findings that he affixed a public customer's name on a switch letter without the customer's knowledge or consent in order to document the customer's previous agreement to a change in investments that had already been executed.

The suspension in any capacity is in effect from October 2, 2006 through November 30, 2006. **(NASD Case #2005002557301)**

Jody Gordon Scheiman (CRD #1124370, Registered Principal, Columbus, Ohio) submitted a Letter of Acceptance, Waiver and Consent in which she was fined \$7,500 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the findings, Scheiman consented to the described sanctions and to the entry of findings that her housekeeper posed as her aunt on a telephone call to obtain information about an insurance policy the aunt owned. The findings stated that Scheiman misled her member firm about the phone call her aunt purportedly made.

The suspension in any capacity was in effect from October 2, 2006 through October 13, 2006. **(NASD Case #2005002264901)**

Lee Gerald Schroeder (CRD #3270789, Registered Principal, Platteville, 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 findings, Schroeder consented to the described sanction and to the entry of findings that he failed to disclose a material fact on his Form U4. The findings stated that Schroeder failed to timely respond to NASD requests for information and failed to appear for an NASD on-the-record interview. **(NASD Case #20050026087-01)**

Nicholas Raymond Sciascia (CRD #2813945, Registered Representative, Howard Beach, New York) was barred from association with any NASD

member in any capacity. The NAC imposed the sanction following appeal of an OHO decision. The sanction was based on findings that Sciascia failed to respond to NASD requests to appear for on-the-record interviews. **(NASD Case #CMS20040069)**

Thomas John Scipione (CRD #809209, Registered Representative, Staten Island, New York) 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 two years. The fine must be paid before Scipione reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Scipione consented to the described sanctions and to the entry of findings that he made a recommendation to a public customer without having reasonable grounds for believing that the recommendation was suitable based upon the customer's financial situation, investment objectives and needs. The findings stated that Scipione submitted to an insurance company an equity indexed annuity application a public customer executed in the state of New York, on which Scipione falsely represented that the customer executed the application in the state of Florida in order to circumvent the requirement that the insurance company be registered in New York to offer its products.

The suspension in any capacity is in effect from October 16, 2006 through October 15, 2008. **(NASD Case #E1020040957-01)**

Harold Stephen Simpson, Sr. (CRD #1071796, Registered Representative, Miramar Beach, 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 findings, Simpson consented to the described sanction and to the entry of findings that he received a \$6,250 check from a public customer for investment purposes but used the funds for his own use and benefit without the customer's authorization or knowledge. The findings stated that Simpson created and delivered a false certificate of stock for a non-existent company to the customer in order to convince the customer that he had invested the funds as directed. The findings also stated that Simpson failed to disclose in writing to his member firm the existence of a brokerage account in which he held a beneficial

interest and failed to notify his member firm in writing of his association with another firm. (NASD Case #2006004213501)

David Parker Smithey (CRD #4137601, Associated Person, Irvine, California) submitted an Offer of Settlement in which he was suspended from association with any NASD member in any capacity for two years and ordered to pay \$525,000, plus interest, in restitution to a public customer. The restitution must be paid before Smithey reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Smithey consented to the described sanctions and to the entry of findings that he participated in private securities transactions and failed to provide prior written notice to, and receive approval from, his member firm.

The suspension in any capacity is in effect from October 16, 2006 through October 15, 2008. (NASD Case #E0220040502-01)

Kenneth Lewis Sojka (CRD #1077371, Registered Principal, Pound Ridge, New York) submitted an Offer of Settlement in which he was fined \$10,000 and suspended from association with any NASD member in any capacity for nine months. The fine must be paid before Sojka reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the allegations, Sojka consented to the described sanctions and to the entry of findings that he directed, encouraged and/or permitted individuals to sign public customers' names on Account Transfer Forms, making the documents false and inaccurate, without the public customers' authorization or consent. The findings stated that Sojka promoted and maintained a workplace environment in which individuals were directed, encouraged and/or permitted to affix customer signatures to firm documents without the customers' authorization or consent. The findings also stated that Sojka settled a customer complaint by paying the customer \$592.40 without his member firm's knowledge or approval.

The suspension in any capacity is in effect from October 16, 2006 through July 15, 2007. (NASD Case #2005002485301)

Andrew Mark Stinson (CRD #4814141, Registered Principal, Fremont, 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 60 days. The fine must be paid before Stinson reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the findings, Stinson consented to the described sanctions and to the entry of findings that he cut a public customer's signature out of a copy of an original state-sponsored 529 plan account application and pasted it in onto an amended application, then submitted it to his member firm for processing.

The suspension in any capacity is in effect from October 16, 2006 through December 14, 2006. (NASD Case #20060049044-01)

Richard Joseph Trivilino (CRD #1498974, Registered Representative, Beaver Falls, 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 findings, Trivilino consented to the described sanction and to the entry of findings that he solicited \$6,850.62 from a public customer for investment purposes, deposited the funds into his personal bank account and converted the funds to his own purposes. (NASD Case #2006004937501)

Brian T. Ungerer (CRD #4414752, Registered Representative, Middletown, Delaware) 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. Without admitting or denying the findings, Ungerer 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 suspension in any capacity is in effect from November 6, 2006 through January 4, 2007. (NASD Case #2005002435801)

Mark Allen Upchurch (CRD #2937074, Registered Representative, Houston, 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 business days. The fine must be paid before Upchurch reassociates with any NASD member following the suspension, or before he requests relief from any statutory disqualification. Without admitting or denying the finding, Upchurch consented to the described sanctions and to the entry of findings that he signed a public customer's name to an account transfer form without her permission.

The suspension in any capacity is in effect from October 16, 2006 through November 27, 2006. (NASD Case #2006004847601)

Dennis Russell Weddle II (CRD #2671849, Registered Representative, Henderson, Nevada) 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 60 days. After consideration of a 51-day suspension his member firm imposed for the same conduct, NASD has determined to credit Weddle with 20 days; accordingly, Weddle is required to serve 40 days of the suspension. Without admitting or denying the findings, Weddle consented to the described sanctions and to the entry of findings that he affixed customer signatures to documents concerning financial planning services.

The suspension in any capacity is in effect from October 16, 2006 through November 24, 2006. (NASD Case #20050012479-01)

Greg B. Whittington (CRD #2544030, Registered Representative, Elkhart, Illinois) submitted a Letter of Acceptance, Waiver and Consent in which he was fined \$5,000 and suspended from association with any NASD member in any capacity for 10 business days. Without admitting or denying the findings, Whittington consented to the described sanctions and to the entry of findings that he engaged in outside business activities, for compensation, without providing prior written notice to his member firm.

The suspension in any capacity was in effect from October 16, 2006 through October 27, 2006. (NASD Case #2005000731201)

Decisions Issued

OHO has issued the following decisions, which have been appealed to or called for review by the NAC as of October 6, 2006. The NAC may increase, decrease, modify or reverse the findings and sanctions imposed in the decision. An initial decision whose time for appeal has not yet expired will be reported in the next *Notice to Members*.

American Funds Distributors, Inc. (CRD #6247, Los Angeles, California) was censured and fined \$5,000,000. The sanctions were based on findings that the firm, as the principal underwriter and distributor of American Funds, entered into yearly sponsorship arrangements with NASD member firms who were top sellers of American Funds. The findings stated that the firm requested and arranged for the payment of specific amounts of trading business to the NASD member firms conditioned on their sales of American Funds.

The firm has appealed this decision to the NAC, and the sanctions are not in effect pending review. (NASD Case #CE3050003)

Anthony Cipriano (CRD #2998665, Registered Representative, West Islip, New York) was fined \$40,000, suspended from association with any NASD member in any capacity for two years and required to re-qualify by examination in all capacities. The sanctions were based on findings that Cipriano made baseless price predictions regarding a security to customers, failed to ensure that his representations to customers had a reasonable basis and failed to disclose material information concerning a securities issuer.

This decision has been appealed to the NAC, and the sanctions are not in effect pending consideration of the appeal. (NASD Case #C0720050029)

Jason Aoam Craig (CRD #4016543, Registered Representative, Washington Township, Michigan) was barred from association with any NASD member in any capacity. The sanction was based on findings that he failed to disclose material information on his Form U4.

This decision has been appealed to the NAC, and the sanction is not in effect pending consideration of the appeal. (NASD Case #E8A2004095901)

Stephen Patrick Dunbar (CRD #2041644, Registered Representative, Atlanta, Georgia) was barred from association with any NASD member in any capacity. The sanction was based on findings that Dunbar's recommendations and trading activity were unsuitable for public customers. The findings stated that Dunbar provided the customers with false and misleading account statements and exercised discretionary authority without the customers' written authorization.

This decision has been appealed to the NAC, and the sanctions are not in effect pending consideration of the appeal. (NASD Case #C0720050050)

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.

Mustapha Youssef Aljaroudi (CRD #3274506, Registered Representative, Miami, Florida) was named as a respondent in an NASD complaint alleging that he engaged in a pattern of misconduct that included falsification of essential public customer information on a new account opening form, thereby causing his firm's books and records to be inaccurate. The complaint alleged that Aljaroudi engaged in an unauthorized sale of stock in a customer's account without the customer's knowledge, authorization or consent. The complaint also alleged that Aljaroudi converted customer funds in that he received a customer's check from a clearing firm, endorsed the check without the customer's knowledge, authorization or consent and deposited the check into his personal bank account without repaying the customer or accounting for the funds. (NASD Case #2005001185301)

Carolyn Sue Callahan (CRD #4115887, Registered Representative, South Bend, Indiana) was named as a respondent in an NASD complaint alleging that she

accepted checks totaling \$45,000 from a public customer to be invested in mutual funds, forged the endorsement of the fund group and deposited the checks into her business checking account. (NASD Case #2005000724301)

Vikram S. Manhas (CRD #2518451, Registered Representative, New York, New York) was named as a respondent in an NASD complaint alleging that without a public customer's knowledge, consent or authorization, Manhas prepared or caused the preparation of forms purportedly signed by the customer, requesting that the customer's assets be transferred into an account Manhas owned. The complaint alleges that Manhas sold the customer's assets and the proceeds from the sales were withdrawn from his account by checks and wire transfers, thereby converting the customer's securities/funds totaling \$240,000. The complaint also alleges that he facilitated the submission of various forms that were purportedly from the customer that contained false information and the customer's forged signature. The complaint further alleges that Manhas failed to respond to NASD requests for information. (NASD Case #20050027081-01)

Masajji Edward Patrick (CRD #4767451, Registered Representative, Chicago, Illinois) was named as a respondent in a complaint alleging that he created fictitious customers using other individuals' Social Security numbers and opened checking accounts in their names. The complaint alleges that Patrick transferred \$57,500 from public customers' dormant accounts to the fictitious checking accounts, thereby using the customers' funds for his own use or benefit, or for the benefit of someone other than the customers, without the customers' knowledge or consent. The complaint also alleges that Patrick failed to respond to NASD requests for information. (NASD Case #2006005120401)

Manuel Rose III (CRD #1424164, Registered Representative, Grand Rapids, Michigan) was named as a respondent in an NASD complaint alleging that he received \$22,000 from a public customer for investment purposes, deposited the funds into his checking account and failed to make any investment on the customer's behalf. The complaint alleges that Rose failed to respond to NASD requests for information. (NASD Case #2005000760301)

Joseph Andrew Zaragosa Jr. (CRD #2417735, Registered Representative, Chicago, Illinois) was named as a respondent in an NASD complaint alleging that he engaged in outside business activity, for compensation, without giving prompt written notice to his member firm. The complaint alleges that Zaragosa effected discretionary transactions in a public customer's account without the customer's prior written authorization, and without his member firm's prior written acceptance of the account as discretionary. The complaint also alleges that Zaragosa effected numerous transactions in a public customer's account without having reasonable grounds for believing that the recommendations were suitable for the customer in view of the size and frequency of the transactions and the nature of the account. The complaint further alleges that Zaragosa failed to submit pieces of email to his member firm for review and approval before sending the correspondence to a public customer. (NASD Case #E8A2002109804)

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

Grayson Financial LLC
Red Bank, New Jersey
(October 23, 2006)

Jersey Shore Trading Group, Inc.
Red Bank, New Jersey
(October 23, 2006)

Firms Suspended for Failure to Supply Financial Information

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

Doral Securities, Inc.
Puerto Nuevo, Puerto Rico
(May 15, 2006 to October 30, 2006)

Dublind Securities, Inc.
Greenwich, Connecticut
(May 10, 2005 to October 5, 2006)

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.)

Amerifinancial fka Fareri Financial Services, Inc.
Boca Raton, Florida
(September 27, 2006 to October 11, 2006)

Black Knight Ventures, Inc.
Tampa, Florida
(October 10, 2006)

Financial Design, Inc.
Baton Rouge, Louisiana
(October 10, 2006)

Kirlin Securities, Inc.
Syosett, New York
(October 20, 2006 to October 23, 2006)

Pacvest Associates, Inc.
Woodstock, Connecticut
(October 20, 2006)

Individuals Barred Pursuant to NASD Rule 9552(h)

Kevin Erik Adams
Fresno, California
(October 24, 2006)

Gilbert Cadavillo Cabusas
Bairwood, New York
(October 31, 2006)

Donovan Britt Craig
Atlanta, Georgia
(October 10, 2006)

Coleman James Flaherty III
South Boston, Massachusetts
(October 4, 2006)

Peter Anthony Mazzara
Chicago, Illinois
(October 2, 2006)

Daniel Lee Rodger
Dallas, Texas
(October 10, 2006)

Maria D. Roldan
Coconut Creek, Florida
(October 6, 2006)

Bryan Keith Smith
Palatka, Florida
(October 31, 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.)

Randall Scott Humphrey
Scottsdale, Arizona
(October 4, 2006)

Christopher Mark Ostoich
Fort Wright, Kentucky
(October 23, 2006)

Jon Manuel Palacios
San Bernardino, California
(October 25, 2006)

Individual 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.)

Francis Hartley-Edwards
San Francisco, California
(October 11, 2006)

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

John F. Helbock
Holmdel, New Jersey
(October 23, 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.)

Dean Russel Baker
Coral Springs, Florida
(October 2, 2006)

Joshua Robinson Ballinger
Ft. Wayne, Indiana
(October 6, 2006)

Gianfranco Carbonara
Flushing, New York
(October 6, 2006)

David Walter Coyman
Long Valley, New Jersey
(October 2, 2006)

John Joseph Donadio
Staten Island, New York
(October 6, 2006)

David P. Gardner
New Rochelle, New York
(October 2, 2006)

Michael Joseph Hernandez
Dallas, Texas
(October 6, 2006)

Scott Fitzgerald Koch
Riverside, Connecticut
(October 2, 2006)

Michael Louis Lieb
Kettering, Ohio
(October 2, 2006)

Jeffery A. Mascio
Highlands Ranch, Colorado
(October 9, 2006)

Padraig Conrad McGlynn
Maspeth, New York
(October 6, 2006)

Sean Fitzgerald Mescall
Denver, North Carolina
(October 9, 2006)

Brett Wilson Pieratt
Highlands Ranch, Colorado
(October 9, 2006)

Daniel Joseph Pyle
E. Atlantic Beach, New York
(October 6, 2006 to October 31, 2006)

Richard Lee Salo
Vancouver, Washington
(October 6, 2006)

Michael Ray Scheurich
Boca Raton, Florida
(October 6, 2006)

Ronald Colon Siracusa
Holbrook, New York
(October 9, 2006)

Roman Thaker
New York, New York
(October 6, 2006)

Robert John Vitale
Parkland, Florida
(October 2, 2006)

Charles William Wannan III
Hicksville, New York
(October 13, 2006 to October 26, 2006)

Jeffrey S. Weick
Margate, Florida
(October 2, 2006)

NASD Fines Citizens Bank Affiliate, CCO Investment Services Corp., \$850,000 For Supervisory, Recordkeeping, Telemarketing, Other Violations

Firm Failed to Implement Procedures Relating to Variable Annuity Sales to Elderly

NASD has fined CCO Investment Services Corp., a wholly-owned subsidiary of Citizens Bank of Rhode Island, a total of \$850,000 for failing to establish, maintain and enforce a reasonably designed supervisory system and written procedures relating to a series of issues-including customer suitability reviews, telemarketing compliance, internal inspections, review of written correspondence, registration of offices and review and approval of 529 Plan business.

NASD found that CCO Investment Services also failed to maintain, among other things, business-related email and records of compensation given to its brokers by issuers of variable contracts or mutual funds.

In addition to the fine, NASD ordered CCO Investment Services to review its supervisory system and procedures concerning the preservation of electronic communications, customer suitability reviews, telemarketing, internal inspections, pre-registration Central Registration Depository (Web CRD) searches, review of written correspondence, registration of offices, and review of customer fund-direct 529 Plan business for compliance with NASD rules and federal securities laws and regulations. The firm was also ordered to undertake a review of the resources it devotes to compliance, assess the adequacy of such resource allocations and make written recommendations concerning its resource needs in order to comply with the laws, regulations and rules concerning those areas.

"Like any securities firm, bank-affiliated broker-dealers must have adequate supervisory systems and controls for ensuring compliance with regulatory requirements," said James S. Shorris, NASD Executive Vice President and Head of Enforcement. "This bank-affiliated firm missed the mark with regard to several important requirements, including some that impacted retirees-an especially vulnerable group for whom NASD rules, the federal securities laws and the telemarketing laws provide valuable protections."

NASD found that from October 2003 through March 2005, CCO Investment Services' suitability reviews of variable annuity contract sales were not reasonably designed to prevent and detect sales practice violations. For example, although the firm utilized surveillance reports and its operations personnel reviewed variable annuity applications before the transactions were completed, it inconsistently provided for reasonable follow-up and review to ensure that noted exceptions were adequately addressed. Moreover, although the firm had some policies related to variable annuity sales to elderly clients, the firm failed to provide for reasonable follow-up and review to ensure that those policies were implemented for these clients. To the extent that the firm had customer suitability review procedures, such as mandating the use of customer financial profile forms, it did not consistently enforce those procedures. As a result, customer information that could have assisted registered persons and the firm in assessing suitability was not always available.

NASD also found several violations relating to the firm's telemarketing efforts. Throughout the relevant period, both CCO Investment Services registered representatives and affiliated bank employees made telephone calls to prospective customers during "call nights." The firm required affiliated bank employees, who were not registered representatives, to use pre-approved scripts and not to discuss specific financial products with customers. But the firm had no supervisory system or written procedures for monitoring compliance with its supervisory procedures in this area. The firm had no reasonable way of even tracking the occurrence of call nights or otherwise monitoring compliance with its procedures. Moreover, during the relevant period, the firm failed to ensure that bank customers called had not registered on the Federal Trade Commission's national Do-Not-Call registry.

In addition, NASD found that the firm's supervisory system and written procedures were not reasonably designed to ensure that searches of the registration records of prospective new hires on Web CRD were performed with the permission of those individuals. During the relevant period, CCO certified to Web CRD that it had obtained the required written consents for its pre-registration searches, but for 239 of those searches the firm had failed to obtain the required consent or lacked the necessary documentation.

In concluding this settlement, CCO neither admitted nor denied the charges, but consented to the entry of NASD's findings.

NASD Fines Oppenheimer and Co. \$800,000 for Failing to Respond to Regulatory Requests, Failing to Report Municipal Transactions Accurately

Firm Also Failed to Retain Internal Email

NASD has fined New York's Oppenheimer & Co. Inc. \$800,000 for failures to respond to regulatory requests for information; failures to report, or to report timely and accurately, thousands of municipal securities transactions, and failure to retain business-related internal email.

In addition to the fine, Oppenheimer is obligated to retain, at its own expense, outside counsel to review, modify, and enhance Oppenheimer's written supervisory procedures related to reporting municipal securities transactions and responding to regulatory requests for information, including requests from NASD.

The sanctions imposed stem from the settlement of a complaint NASD filed against Oppenheimer in April 2005.

"Firms must respond timely and completely to regulatory requests, report transactions timely and accurately, and maintain business-related electronic communications," said James S. Shorris, NASD Executive Vice President and Head of Enforcement. "Oppenheimer repeatedly failed to comply with these fundamental regulatory obligations."

NASD found that Oppenheimer failed to respond timely and fully to a September 2004 NASD request that it provide information about its retention of electronic communications for 20 employees who traded municipal securities and whose emails were therefore necessary to an NASD investigation into Oppenheimer's trade reporting deficiencies. In May 2005, Oppenheimer responded in writing to only one portion of the September 2004 request, but never provided information responsive to the balance of NASD's request.

Oppenheimer also failed to respond timely to an August 2003 request for trade confirmations for municipal securities transactions. NASD renewed its request for

confirmations on three occasions, yet Oppenheimer did not produce all confirmations until more than a year after the original request.

NASD also found that from January 2003 through May 2004, Oppenheimer failed to timely report to the Municipal Securities Rulemaking Board (MSRB) more than 6,100 interdealer municipal securities transactions and eventually reported hundreds of these transactions inaccurately. In addition, during May and part of June 2003, the firm failed to accurately report to MSRB the price, time, commission or capacity in which it acted in more than 1,500 customer trades. During the same time period, it failed to report more than 600 municipal securities transactions with customers.

In settling these matters, Oppenheimer neither admitted nor denied the charges, but consented to the entry of NASD's findings.

McLaughlin, Piven and Vogel Securities Agrees to Repay Customers Overcharged for Transferring Accounts

NASD Fines Firm \$50,000, Orders Compliance Review by Independent Consultant

NASD announced that McLaughlin, Piven and Vogel Securities, Inc. (MPV) of New York has agreed to pay restitution to customers who were charged excessive and unreasonable fees in connection with the transfer of their brokerage accounts to other broker-dealers through the Automated Customer Account Transfer System (ACATS). NASD has identified more than 1,500 customers who were overcharged.

ACATS is administered by the National Securities Clearing Corporation. It was designed to expedite the transfer of customer accounts between participants in a registered clearing agency, to alleviate the demands of manual processing of account transfers on firms and to reduce costs.

NASD also fined MPV \$50,000 and ordered the firm to retain an independent consultant to determine the amount of restitution due customers and to review and make recommendations concerning the adequacy of the firm's current policies, systems, procedures and training concerning compliance with NASD's rules relating to charges for services performed.

"Fees and charges assessed by firms must be reasonable and, in the case of account transfers, bear a relationship to the actual cost of the services provided," said James S. Shorris, NASD Executive Vice President and Head of Enforcement. "In this case, the firm attributed a portion of the ACATS fees it charged—as much as \$295—to its costs of investigating brokers whose customers had left the firm. This was an utterly improper assessment of an ACATS fee and was excessive, given that MPV was charged as little as \$35 by its clearing firm to process these account transfers."

NASD sampled more than 1,600 registered firms and found that ACATS fees imposed on customers typically run no higher than \$50, with the firm retaining \$25 or less of that fee.

NASD rules require that charges for services be "reasonable and not unfairly discriminatory between customers." Additionally, NASD has advised registered firms, through Notices to Members, that charges for services must be fair under the relevant circumstances, that each member "should be prepared to justify that its prices are fair as to each customer and transaction" and that ACATS fees should be related to the actual costs of the account transfers.

NASD found that between April 2002 and September 2006, MPV violated NASD's rules by charging more than 1,500 customer accounts excessive and unreasonable account transfer fees. Between April 2002 and mid-April 2006, the firm charged customers \$295 per account transferred. MPV kept, after clearing firm charges, between \$235 and \$260 per account. Between mid-April and September 2006, the firm charged customers \$195 per account transferred and retained, after clearing charges, \$135 per account.

MPV charged the high transfer fees, in part, to offset the firm's costs of investigating departing brokers, to determine whether they had made false statements to persuade customers to transfer their accounts in violation of the departing brokers' employment agreements. NASD found that the respective \$295 and \$195 transfer fees were excessive, unreasonable and largely unrelated to MPV's actual costs of processing account transfers through ACATS. Any costs associated with investigating possible impropriety by departing brokers were unrelated to MPV's actual costs of effecting account transfers and may not be shifted to the customers.

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

NASD Fines Hedge Fund Manager \$2.25 Million for Deceptive Market Timing in Variable Annuities

NASD's Largest Market Timing Fine Ever Against an Individual; Probe Continues Into Activities of Individual Brokers

NASD imposed its largest fine ever against an individual for market timing—a \$2.25 million sanction against hedge fund manager Paul Saunders, a registered broker who is Chairman, CEO and majority owner of James River Capital Corporation (JRCC) of Richmond, VA. The fine, for using deceptive practices to market time through variable annuities, includes disgorgement of approximately \$750,000 in illicit profits. NASD also suspended Saunders for 60 days.

NASD's investigation into the activities of the brokers who assisted Saunders' market timing is continuing.

"Deceptive market timing designed to exceed prospectus limitations and evade insurance company and mutual fund restrictions not only violates ethical standards but may also harm investors," said James S. Shorris, Executive Vice President and Head of Enforcement. "The enforcement action announced today makes clear that brokers, including those who operate as hedge fund managers, will be held accountable for this kind of misconduct and will be required to disgorge their profits and pay a substantial penalty."

JRCC is general partner and trading manager of the Jazzman Fund, a hedge fund established specifically to engage in market timing. After personally investing in Jazzman, Saunders, through JRCC, created 19 limited partnerships under Jazzman to increase the hedge fund's ability to market time mutual fund sub-accounts of variable annuities. While each Jazzman partnership appeared to be a separate entity, with a different name and tax identification number, the partnerships all had common owners—a fact that Saunders did not disclose to insurance companies that offered the variable annuities.

NASD found that from October 2001 through September 2003, Saunders used these Jazzman partnerships to engage in numerous deceptive practices to evade attempts by insurance companies to block or restrict his market timing in sub-accounts of variable annuities.

Saunders opened 20 different accounts for the Jazzman partnerships at one broker-dealer and commenced market timing through variable annuity sub-accounts, sometimes simultaneously purchasing contracts and trading in the same annuity through several Jazzman partnerships. After receiving communications from insurance companies restricting further market timing, the Jazzman hedge fund, under Saunders' direction, used three deceptive practices to continue market timing:

- Saunders purchased contracts in the same variable annuity for other Jazzman partnerships and continued trading through those contracts;
- Saunders obtained additional contracts in the same variable annuity, but changed the name of the annuitant. All of the annuitants were actually employees of entities Saunders controlled; and
- When certain insurance companies rejected an annuity contract because it was purchased with a large initial investment, Saunders purchased another contract with a much smaller initial investment. When that contract was accepted, Saunders transferred funds from accounts of other related Jazzman partnerships to the accepted contract and then began market timing in the contract's sub-accounts.

These practices enabled Jazzman to execute approximately 1,000 variable annuity transactions, well in excess of insurance company limits for any single entity. Saunders personally made approximately \$750,000 in illicit profits from the deceptive conduct.

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