

July 29, 2003

Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

Re: File No. SR-NASD-2003-92 - Borrowing From Or Lending To Customers

Dear Ms. England:

This letter responds to the comment letter submitted by the North American Securities Administrators Association ("NASAA")¹ in response to the publication in the *Federal Register* of Notice of Filing of SR-NASD-2003-92 to adopt NASD Rule 2370 to govern certain lending arrangements between registered persons and customers.²

NASAA states that it endorses further restrictions being placed on loans between registered persons and customers, since such arrangements can be problematic. NASAA notes that the potential for conflict is particularly great when business associates enter into loan arrangements outside the normal business relationship. NASAA additionally notes a NASAA Statement of Policy that prohibits an agent of a broker-dealer from engaging in "the practice of lending or borrowing money or securities from a customer."

In arriving at the proposed rule change, NASD, like NASAA, considered that lending arrangements between registered persons and customers can be problematic and that conflicts can arise when registered persons borrow from or lend to customers. After substantial discussions with its members, NASD arrived at proposed Rule 2370, which would give members the ability to prohibit all customer-broker lending arrangements if they wish to do so, but would also establish strict conditions under which customer-broker lending arrangements could take place if members wish to permit them.

Thus, proposed Rule 2370 will permit members to prohibit all customer-broker lending arrangements. However, if members decide to permit customer-broker lending arrangements,

¹ The list of commenters is attached as Exhibit 1.

² Release No. 34-48093 (June 26, 2003); 68 F.R. 39608 (July 2, 2003). The public comment period announced in the *Federal Register* expired on July 23, 2003.

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they must have written procedures in place evidencing their customer loan policy, and loans will be limited to the types of lending arrangements described in proposed Rule 2370. With the aid of its members, NASD staff identified five types of lending arrangements that might not be problematic because of the relationship between the registered person and the customer. Thus, even if a member permits its registered persons to lend to or borrow from firm customers, the rule limits such arrangements to five permissible arrangements: the customer is a member of the registered person's immediate family; the customer is in the business of lending money; the customer and the registered person are both registered persons of the same firm; the lending arrangement is based on a personal relationship outside of the broker-customer relationship; or the lending arrangement is based on a business relationship outside of the broker-customer relationship.

In addition to limiting customer-broker loans to five permissible types of arrangements, proposed Rule 2370 provides additional safeguards against unethical lending arrangements by establishing a "notice and approval requirement." Thus, under proposed Rule 2370, registered persons will be required to give their firms prior notice of a loan, and firms will be required to pre-approve each loan in writing. These requirements will enable a member, to the extent it permits these loan arrangements, to assess the nature of each proposed arrangement and decide whether to approve it. They also will enhance NASD's ability to review these arrangements during the examination process.

NASD believes that this regulatory framework addresses the conflict and other problems inherent in customer-broker lending arrangements by (1) giving members the ability to prohibit such loans altogether; (2) where permitted, limiting such loans to five permissible lending arrangements; and (3) requiring firms to maintain written procedures allowing such lending arrangements consistent with the rule; and (4) establishing prior notice and approval requirements.

NASD hereby extends the time for Securities and Exchange Commission action on the above-referenced rule filing to September 1, 2003.

Very truly yours,

Shirley H. Weiss,
Associate General Counsel

cc: Christopher Solgan
T.R. Lazo

EXHIBIT 1

1. North American Securities Administrators Association (July 23, 2003)