

August 10, 2004

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-2004-121 – Amendments to NASD’s Minor Rule Violation Plan

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed please find the above-numbered rule filing. Also enclosed is a 3-1/2” disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Shirley H. Weiss, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8844; e-mail shirley.weiss@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Marc Menchel
Executive Vice President
and General Counsel

Enclosures

File No. SR-NASD-2004-121
Consists of 39 Pages
August 10, 2004

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.

Form 19b-4

Proposed Rule Change

by

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), the National Association of Securities Dealers, Inc. ("NASD") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change to amend NASD Interpretative Material 9216 ("IM-9216") to expand the list of violations eligible for disposition under NASD's Minor Rule Violation Plan ("MRVP") to include failure to timely submit amendments to the Form U5, as required by Article V, Section 3(a) of the NASD By-Laws. Below is the text of the proposed rule change. Proposed new language is underlined; deletions are in brackets.¹

* * * * *

9200. DISCIPLINARY PROCEEDINGS

* * * * *

IM-9216. Violations Appropriate for Disposition Under Plan Pursuant to SEC Rule 19d-1(c)(2)

—Rule 2210(b) and (c) and Rule 2220(b) and (c)—Failure to have advertisements and sales literature approved by a principal prior to use, failure to maintain separate files of advertisements and sales literature containing required information, and failure to file communications with NASD within the required time limits.

—Rule 3360—Failure to timely file reports of short positions on Form NS-1.

¹ On February 10, 2004, NASD proposed additional amendments to its MRVP. See SR-NASD-2004-025. NASD would amend the rule text set forth in this rule change in the event the Commission approves SR-NASD-2004-025.

—Rule 3110—Failure to keep and preserve books, accounts, records, memoranda, and correspondence in conformance with applicable laws, rules, regulations and statements of policy promulgated thereunder, and with NASD Rules.

—Rule 8211, Rule 8212, and Rule 8213—Failure to submit trading data as requested.

—Article IV—Failure to timely submit amendments to Form BD.

—Article V—Failure to timely submit amendments to Form [U-4] U4.

—Article V—Failure to timely submit amendments to Form U5.

—Rule 1120—Failure to comply with continuing education requirements (Firm Element).

—Rule 3010(b)—Failure to timely file reports pursuant to the Taping Rule.

—Rule 3070—Failure to timely file reports.

—Rule 4619(d)—Failure to timely file notifications pursuant to SEC Regulation M.

—Rules 4632, 4642, 4652, 6240, 6420, 6620, 6650, and 6720—Transaction reporting in equity, convertible debt, and high yield securities.

—Rules 6130 and 6170—Transaction reporting to ACT.

—Rules 6954 and 6955—Failure to submit data in accordance with OATS.

—Rule 11870—Failure to abide by customer account transfer contracts.

—SEC Rule 11Ac1-4—Failure to properly display limit orders.

—SEC Rule 11Ac1-1(c)(5)—Failure to properly update published quotes in certain ECNs.

—SEC Exchange Act Rule 17a-5—Failure to timely file FOCUS reports and annual audit reports.

—SEC Exchange Act Rule 17a-10—Failure to timely file Schedule I.

—MSRB Rule A-14—Failure to pay annual fee.

—MSRB Rule G-12—Failure to abide by uniform practice rules.

—MSRB Rule G-14—Failure to submit reports.

—MSRB Rule G-36—Failure to timely submit reports.

—MSRB Rule G-37—Failure to timely submit reports for political contributions.

—MSRB Rule G-38—Failure to timely submit reports detailing consultant activities.

* * * * *

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) The NASD Regulation, Inc. Board of Directors approved the proposed rule change on July 21, 2004, which authorized the filing of the rule change with the SEC. Counsel for The Nasdaq Stock Market ("NASDAQ") and NASD Dispute Resolution have been provided an opportunity to consult with respect to the proposed rule change, pursuant to the Plan of Allocation and Delegation of Functions by NASD to its Subsidiaries. The NASD Board of Governors had an opportunity to review the proposed rule change at its meeting on July 22, 2004. No other action by NASD is necessary for the filing of the proposed rule change. Section 1(a)(iii) of Article VII of the NASD By-Laws permits the NASD Board of Governors to amend NASD interpretative materials without recourse to the membership for approval.

NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 30 days following Commission approval. The effective date will be 30 days following publication of the Notice to Members announcing Commission approval.

(b) Questions regarding this rule filing may be directed to Shirley H. Weiss, Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8844.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Background

In 1984, the SEC adopted amendments to Rule 19d-1(c) under the Exchange Act to allow self-regulatory organizations to adopt, with SEC approval, plans for the disposition of minor violations of rules.² In 1993, pursuant to SEC Rule 19d-1(c), NASD established an MRVP.³ See NASD Rule 9216(b). In 2001, the SEC approved significant amendments to NASD's MRVP⁴ and, in February 2004, NASD proposed additional amendments to its MRVP.⁵

The purpose of the MRVP is to provide for a meaningful sanction for a minor or technical violation of a rule when the initiation of a disciplinary proceeding through the formal complaint process would be more costly and time-consuming than would be warranted. Inclusion of a rule in NASD's MRVP does not mean it is an unimportant rule; rather, a minor or technical violation of the rule may be appropriate for disposition under the MRVP. NASD retains the discretion to bring full disciplinary proceedings.

Rule 9216(b) authorizes NASD to impose a fine of \$2,500 or less on any member or

² See Exchange Act Rel. No. 21013 (June 1, 1984), 49 FR 23833 (June 8, 1984).

³ See Exchange Act Rel. No. 32076 (Mar. 31, 1993), 58 FR 18291 (Apr. 8, 1993); see also *Notice to Members 93-42* (July 1993).

⁴ See Exchange Act Rel. No. 44512 (July 3, 2001), 68 FR 36812 (July 13, 2001).

⁵ See SR-NASD-2004-025.

associated person of a member for a violation of any of the rules specified in IM-9216. NASD staff reviews the number and seriousness of the violations, as well as the previous disciplinary history of the respondent to determine if a matter is appropriate for disposition under the MRVP and to determine the amount of the fine. Once NASD has brought a minor violation of a rule against an individual or member firm, NASD may, at its discretion, issue progressively higher fines for all subsequent minor violations of rules within the next 24-month period or initiate more formal disciplinary proceedings.⁶

Discussion

NASD is proposing to amend its MRVP to include the failure to timely submit amendments to the Form U5, as required by Article V, Section 3(a) of the NASD By-Laws. Including this violation would be consistent with the current MRVP, which includes failure to timely submit amendments to the Form U4, as required by Article V, Section 2(c) of the NASD By-Laws, and failure to timely submit amendments to the Form BD, as required by Article IV, Section 1(c) of the NASD By-Laws. Expanding NASD's MRVP to include failure to timely submit amendments to the Form U5 will give NASD's Department of Enforcement the additional flexibility in resolving these violations as it now has regarding the failure to timely submit amendments to the Form U4 and Form BD.⁷

(b) Statutory Basis

⁶ See *Notice to Members 04-19* (March 2004) (NASD Releases Minor Rule Violation Plan (MRVP) Guidelines), which provides interested parties with guidance concerning the application of NASD's MRVP to each of the rules under the Plan, as specified in NASD IM-9216. This guidance includes identifying the factors to be considered in determining whether to dispose of an action under the MRVP and discussing the appropriate levels for fines.

⁷ This rule filing also changes "U-4" to "U4," to be consistent with the most recent amendments to the Form U4.

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that NASD rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that the proposed rule change is consistent with Section 15A(b)(7) of the Act in that it provides for the appropriate discipline for violation of NASD rules. The rule change also is consistent with Section 15A(b)(8) of the Act in that it furthers the statutory goals of providing a fair procedure for disciplining members and associated persons. NASD believes that the addition of this violation to the MRVP will provide NASD staff with the ability to impose a meaningful sanction for violations of this rule that warrant more than a Letter of Caution, but do not necessarily rise to a level meriting a full disciplinary proceeding.

4. Self-Regulatory Organization's Statement on Burden on Competition

NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

In March 2004, NASD published *Notice to Members 04-23* requesting comment on amending its MRVP to include failure timely to submit amendments to the Form U5 and adopting a rule to create an inactive disclosure review registration status. Five of the seven commenters commented on the proposed amendment to NASD's MRVP, and all five commenters supported the proposal.⁸ One commenter suggested that fines for late Form U5

⁸ Two commenters addressed the "inactive disclosure" issue, but did not address the MRVP issue.

filings be based on the percentage of assets under management to encourage compliance. NASD notes that its MRVP is restricted to fines of \$2,500 or less. Additionally, rather than relying on a formula to impose sanctions pursuant to its MRVP, NASD considers the facts and circumstances of each cases in determining appropriate sanctions. Moreover, NASD retains the discretion to bring full disciplinary action against a respondent, which may involve higher monetary sanctions, when the facts and circumstances of the violation warrant a formal complaint.

6. Extension of Time Period for Commission Action

NASD does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibits

1. Completed notice of proposed rule change for publication in the Federal Register.
2. *Notice to Members 04-23*.
3. Comments received in response to *Notice to Members 04-23*.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD

BY: _____
Marc Menchel, Executive Vice President and General Counsel
NASD, Regulatory Policy and Oversight

Date: August 10, 2004

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-

; File No. SR-NASD-2004-121)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Proposed Amendments to NASD's Minor Rule Violation Plan

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on _____, 2004, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS OF SUBSTANCE OF THE PROPOSED RULE CHANGE

NASD is filing with the Commission a proposed rule change to amend NASD Interpretative Material 9216 ("IM-9216") (Violations Appropriate for Disposition Under the Plan Pursuant to SEC Rule 19d-1(c)(2)) to expand the list of violations eligible for disposition under NASD's Minor Rule Violation Plan ("MRVP") to include failure to timely submit amendments to the Form U5, as required by Article V, Section 3(a) of the NASD By-Laws. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.³

¹ 15 U.S.C. § 78s(b)(1).

² 17 CFR 240.19b-4.

³ On February 10, 2004, NASD proposed additional amendments to its MRVP. See SR-NASD-2004-025. NASD would amend the rule text set forth in this rule change in the event the Commission approves SR-NASD-2004-025.

* * * * *

9200. DISCIPLINARY PROCEEDINGS

* * * * *

IM-9216. Violations Appropriate for Disposition Under Plan Pursuant to SEC Rule 19d-1(c)(2)

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* * * * *

II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its filing with the Commission, NASD included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV

below. NASD has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Background

In 1984, the SEC adopted amendments to Rule 19d-1(c) under the Exchange Act to allow self-regulatory organizations to adopt, with SEC approval, plans for the disposition of minor violations of rules.⁴ In 1993, pursuant to SEC Rule 19d-1(c), NASD established an MRVP.⁵ See NASD Rule 9216(b). In 2001, the SEC approved significant amendments to NASD's MRVP⁶ and, in February 2004, NASD proposed additional amendments to its MRVP.⁷

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(b) Statutory Basis

⁸ See Notice to Members 04-19 (March 2004) (NASD Releases Minor Rule Violation Plan (MRVP) Guidelines), which provides interested parties with guidance concerning the application of NASD's MRVP to each of the rules under the Plan, as specified in NASD IM-9216. This guidance includes identifying the factors to be considered in determining whether to dispose of an action under the MRVP and discussing the appropriate levels for fines.

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(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

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filings be based on the percentage of assets under management to encourage compliance. NASD notes that its MRVP is restricted to fines of \$2,500 or less. Additionally, rather than relying on a formula to impose sanctions pursuant to its MRVP, NASD considers the facts and circumstances of each cases in determining appropriate sanctions. Moreover, NASD retains the discretion to bring full disciplinary action against a respondent, which may involve higher monetary sanctions, when the facts and circumstances of the violation warrant a formal complaint.

III. DATE OF EFFECTIVENESS OF THE PROPOSED RULE CHANGE AND TIMING FOR COMMISSION ACTION

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- A. by order approve such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Comments also may be submitted electronically at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File No. SR-NASD -2004-121. This file number should be

included on the subject line if e-mail is used. To help us process and review comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods.

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of NASD. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland
Deputy Secretary