

Notice to Members

APRIL 2003

SUGGESTED ROUTING

Legal & Compliance
Operations
Principals
Registration
Registered Representatives
Senior Management
Training

KEY TOPICS

Registration Rules

INFORMATIONAL

Registration Rules

Technical Changes to the NASD Registration Rules
Effective Immediately

Executive Summary

On February 26, 2003, NASD filed with the Securities and Exchange Commission (SEC) for immediate effectiveness changes to the NASD Registration Rules.¹ The changes are technical in nature and include, among other things, removing references to old NASD forms and registration categories, deleting provisions regarding outdated grandfathering clauses, deleting duplicative provisions, and combining certain provisions to eliminate redundancies in the rule language. The text of the amendments and *Federal Register* version of the SEC Notice are attached (see Attachments A and B). For a detailed description of the amendments, members should review the attached SEC Notice (see Attachment B).

Questions/Further Information

Questions concerning this *Notice* may be directed to Afshin Atabaki, Attorney, Office of General Counsel, NASD Regulatory Policy and Oversight, at (202) 728-8902.

Background

As part of NASD's rule modernization initiative, NASD identified certain registration rules that were antiquated and needed updating to reflect changes in the regulatory landscape. The amendments clarify and clean up existing rules to reduce burdens on the industry resulting from these outdated registration requirements. These rule changes include:

- ♦ amendments to Rules 1021(a) and 1031(a) to permit a member to maintain or make application for the registration of a principal or representative who performs back-office operations;
- ♦ amendment to Rule 1021(d)(1) to reflect that members are required to submit an amended "Uniform Application for Securities Industry Registration or Transfer" (Form U-4) rather than an "elevation form," which was an outdated form;
- ♦ deletion of Rule 1021(d)(3) because it inaccurately suggested that an applicant who did not take the examination within 90 days or failed the examination could submit a new form and continue to function as a principal until qualified. This was inconsistent with Rule 1021(d)(1), which states that in no event may a person function as a principal beyond the initial 90-day period;
- ♦ amendment to Rule 1021(e) to clarify that existing members as well as new applicants are required to have at least two principals with respect to each aspect of their investment banking and securities business;
- ♦ removal of the reference to "financial principal" from Rule 1022(a)(3) because it related to an examination that is no longer administered;
- ♦ combining Rules 1022(a)(4), (5), and (6) to eliminate certain redundancies in the language and to clarify that a person registered solely as a general securities principal is not automatically qualified to function as a municipal securities principal or municipal fund securities limited principal;
- ♦ amendment to Rule 1022(g)(2)(A) to state that a person registered solely as a limited principal—general securities sales supervisor shall not be qualified to function in a principal capacity with responsibility over any of the areas of business not described in that rule. This change will clarify that such persons may be registered in other categories, if applicable;
- ♦ deletion of Rules 1032(a)(2)(A)–(D) and 1032(a)(2)(F) because these sections are no longer relevant to a majority of NASD members and, if necessary, the staff may provide waivers;
- ♦ amendment to Rule 1032(a)(2)(G) to reflect the Financial Services Authority's (FSA) new authorization and approval process;
- ♦ deletion of Rule 1032(g)(3) because most persons who were eligible for grandfathering have been processed and, if necessary, the staff may provide waivers to new applicants;
- ♦ removal of the phrase "on a pass/fail basis only" from Rule 1070(c) because NASD provides more than just pass/fail information to members;

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- ▶ amendment to Rule 1070(e) to clarify that although age or physical infirmity will not individually of themselves constitute sufficient grounds to waive an examination, experience in an ancillary field may be sufficient grounds to waive an examination; and
 - ▶ replacement of the terms “Application for Classification as a Foreign Associate” in Rule 1100(b) with the terms “Uniform Application for Securities Industry Registration or Transfer,” which is the current application.

For a more detailed description of the amendments, members should review the attached SEC Notice.

Endnote

- 1 See Securities Exchange Act Release No. 47433 (March 3, 2003), 68 FR 11424 (March 10, 2003) (notice of filing and immediate effectiveness of File No. SR-NASD-2003-24) (“SEC Notice”).

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ATTACHMENT A

New language is underlined; deletions are in brackets.

1000. Membership, Registration and Qualification Requirements

1020. Registration of Principals

1021. Registration Requirements

(a) All Principals Must Be Registered

All persons engaged or to be engaged in the investment banking or securities business of a member who are to function as principals shall be registered as such with [the Association] NASD in the category of registration appropriate to the function to be performed as specified in Rule 1022. Before their registration can become effective, they shall pass a Qualification Examination for Principals appropriate to the category of registration as specified by the Board of Governors. A member shall not maintain a principal registration with [the Association] NASD for any person (1) who is no longer active in the member's investment banking or securities business, (2) who is no longer functioning as a principal, or (3) where the sole purpose is to avoid the examination requirement prescribed in paragraph (c). A member shall not make application for the registration of any person as principal where there is no intent to employ such person in the member's investment banking or securities business. A member may, however, maintain or make application for the registration as a principal of a person who performs legal, compliance, internal audit, back-office operations, or similar responsibilities for the member or a person engaged in the investment banking or securities business of a foreign securities affiliate or subsidiary of the member.

(b) through (c) No Change.

(d) Application for Principal Status

(1) Any person associated with a member as a Registered Representative whose duties are changed by the member so as to require registration in any principal classification shall be allowed a period of 90 calendar days following the change in his duties during which to pass the appropriate Qualification Examination for Principals. Upon elevation, the member shall submit to [the Association] NASD an [elevation form] amended "Uniform Application for Securities Industry Registration or Transfer" [designated by the Board of Governors] and the

applicable fees. In no event may a person function as a Principal beyond the initial 90 calendar day period following the change in his duties without having successfully passed the appropriate Qualification Examination.

(2) No Change.

[(3) If an applicant does not take the examination within the ninety calendar day period or if the applicant fails the examination, a new principal elevation form and examination fee shall be required.]

(e) Requirement of Two Registered Principals for [New Applicants for Membership] Members

(1) An [applicant for membership in the Association] NASD member, except a sole proprietorship, shall have at least two officers or partners who are [qualified to become] registered as principals with respect to each aspect of the [applicant's] member's investment banking and securities business pursuant to the applicable provisions of Rule 1022[(a), (d) and (e), whichever are applicable, before it shall be admitted to membership]. This requirement applies to persons seeking admission as members and existing members.

(2) through (3) No Change.

1022. Categories of Principal Registration

(a) General Securities Principal

(1) through (2) No Change.

(3) Except as provided in Rule 1021(c), a person who was registered with [the Association] NASD as a Principal [or a Financial Principal,] shall not be required to pass a Qualification Examination for General Securities Principal and shall be qualified as a General Securities Principal.

(4) A person registered solely as a General Securities Principal shall not be qualified to function as a Limited Principal—Financial and Operations; Limited Principal—Registered Options and Security Futures; Limited Principal—General Securities Sales Supervisor; Municipal Securities Principal, or Municipal Fund Securities Limited Principal, unless [he] that person is also qualified and registered as such [pursuant to paragraph (b)].

[(5) A person registered solely as a General Securities Principal shall not be qualified to function as a Registered Options Principal unless he is also qualified and registered as such pursuant to the provisions of paragraph (f).]

[(6) A person qualified solely as a General Securities Principal shall not be qualified to be registered as a Limited Principal—General Securities Sales Supervisor unless he is also qualified and registered as such pursuant to the provisions of paragraph (g)(1).]

(b) Limited Principal—Financial and Operations

(1) through (2) No Change.

[(3) Except as provided in Rule 1021(c), a person designated pursuant to the provisions of subparagraph (1) hereof shall not be required to take the Limited Principal—Financial and Operations Examination and shall be qualified for registration as a Limited Principal—Financial and Operations if:

(A) such person had been performing the functions of a Limited Principal—Financial and Operations as defined in subparagraph (2) hereof on or before September 1, 1972; or

(B) such person was registered with the Association as a Financial Principal.]

(4) Renumbered as (3)

(c) through (e) No Change.

(f) Limited Principal—Registered Options and Security Futures [Principals]

No Change to rule language.

(g) Limited Principal—General Securities Sales Supervisor

(1) No Change.

(2) A person registered in this category solely on the basis of having passed the Qualification Examination for Limited Principal—General Securities Sales Supervisor shall NOT be qualified to:

(A) [be registered in any other category of principal registration] function in a principal capacity with responsibility over any area of business activity not prescribed in subparagraph (1);

(B) through (C) No Change.

(3) No Change.

(h) Limited Principal—Government Securities

(1) All persons associated with a member not previously registered as a principal who are to function as government securities principals shall be registered as such with NASD.

(2) Each person associated with a member must be registered as a Limited Principal—Government Securities if such person is:

(A) engaged in the management or supervision of the member's government securities business, including:

(i) underwriting, trading or sales of government securities;

(ii) financial advisory or consultant services for issuers in connection with the issuance of government securities;

(iii) research or investment advice, other than general economic information or advice, with respect to government securities in connection with the activities described in (i) and (ii) above;

(iv) activities other than those specifically described above that involve communication, directly or indirectly, with public investors in government securities in connection with the activities described in (i) and (ii) above; or

(B) responsible for supervision of:

(i) the processing and clearance activities with respect to government securities; or

(ii) the maintenance of records involving any of the activities described in paragraph (2)(A) above.

(3) Notification of Principal Status

A member shall promptly notify NASD when an individual not previously registered with the member as a principal assumes the duties of a principal on the form designated by the Board accompanied by the applicable fees.

IM-1022-1. Limited Principal—Registered Options and Security Futures [Principals]

No Change to rule language.

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1030. Registration of Representatives

1031. Registration Requirements

(a) All Representatives Must Be Registered

All persons engaged or to be engaged in the investment banking or securities business of a member who are to function as representatives shall be registered as such with [the Association] NASD in the category of registration appropriate to the function to be performed as specified in Rule 1032. Before their registration can become effective, they shall pass a Qualification Examination for Representatives appropriate to the category of registration as specified by the Board of Governors. A member shall not maintain a representative registration with [the Association] NASD for any person (1) who is no longer active in the member's investment banking or securities business, (2) who is no longer functioning as a representative, or (3) where the sole purpose is to avoid the examination requirement prescribed in paragraph (c). A member shall not make application for the registration of any person as representative where there is no intent to employ such person in the member's investment banking or securities business. A member may, however, maintain or make application for the registration as a representative of a person who performs legal, compliance, internal audit, back-office operations, or similar responsibilities for the member, or a person who performs administrative support functions for registered personnel, or a person engaged in the investment banking or securities business of a foreign securities affiliate or subsidiary of the member.

(b) through (c) No Change.

1032. Categories of Representative Registration

(a) General Securities Representative

(1) No Change.

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

[(A) Any person who was registered with the Association as a Representative prior to September 1, 1974, shall be qualified to be registered with the Association as a General Securities Representative.]

[(B) A person who applied for registration as a Representative prior to September 1, 1974, and who become registered as a Representative prior to April 1, 1975 by virtue of having passed the Qualification Examination for Representatives (Test Series 1) shall be qualified to be registered as a General Securities Representative.]

[(C) A person who applied for registration as a Representative on or after September 1, 1974, or who registered as a Representative on or after April 1, 1975 by virtue of having passed the Qualification Examination for Registered Representatives (Test Series 1) shall be qualified to be registered only as a Limited Representative—Investment Company and Variable Contracts Products and as a Limited Representative—Direct Participation Programs as defined in paragraph (b) and (c) hereof.]

[(D) A person who was registered as a Registered Representative after September 1, 1974 by virtue of having passed the General Securities Representative Examination (Test Series 7) shall be qualified to be registered as a General Securities Representative.]

(E) Renumbered as (A)

[(F) A person who was registered as a Registered Representative for Sale of Variable Contracts Only shall be qualified to be registered as a Limited Representative—Investment Company and Variable Contracts Products.]

[(G)] (B) A person [registered and in good standing with] who is authorized or approved to conduct business in accordance with the requirements of The [Securities and Futures] Financial Services Authority and having passed the Modified General Securities Representative Qualification Examination [for United Kingdom Representatives] shall be qualified to be registered as a General Securities Representative except that such person's activities in the investment banking or

securities business may not involve the solicitation, purchase and/or sale of municipal securities as defined in Section 3(a)(29) of the Act.

(H) through (I) Renumbered as (C) through (D)

(3) No Change.

(b) through (e) No Change.

(f) Limited Representative—Equity Trader

(1) No Change.

(2) Before registration as a Limited Representative—Equity Trader as defined in subparagraph (1) hereof may become effective, an applicant must:

(A) No Change.

(B) pass an appropriate Qualification Examination for Limited Representative—Equity Trader. [Any person who was performing any of the activities described in paragraph (f)(1) above on or prior to May 1, 1998 and who has filed an application to take this examination by August 31, 1998 must pass the examination by May 1, 2000. Any person who is eligible for this extended qualification period and who fails this examination during the twenty-four (24) month time period commencing on May 1, 1998 and ending on May 1, 2000 must wait thirty (30) days from the date of failure to take the examination again. Any person, other than a person who is eligible for the extended qualification period, who files an application to take this qualification examination after May 1, 1998 must pass this examination before conducting such activities as described in paragraph (f)(1) above. In no event may a person who is eligible for the extended qualification period function as an Equity Trader beyond the 24-month period without having successfully passed the appropriate qualification examination.]

(g) Limited Representative—Government Securities

(1) through (2) No Change.

[(3) A person who has been performing the functions of a Limited Representative—Government Securities on or before April 1, 1996, may register as such without first meeting the requirement of subparagraph (1)(B) above unless:

(A) such person is currently subject to a statutory disqualification as defined in Section 3(a)(39) of the Act or

(B) during the past ten years before the effective date of that requirement was the subject of a suspension or fine of \$5,000 or more by the Association, the Securities and Exchange Commission, the Commodity Futures Trading Commission, state securities commission, foreign financial regulatory authority, or any other regulatory organization responsible for the investment banking or securities business.]

(h) No Change.

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1070. Qualification Examinations and Waiver of Requirements

(a) through (b) No Change.

(c) Examination results shall be reported to member firms [on a pass/fail basis only] and may be accompanied by an analysis of the candidate's performance on the examination. Passing scores assigned to each examination series shall be determined by the Board of Governors, or its designee.

(d) [An applicant cannot receive assistance while taking the examination. Each applicant shall certify to the Board of Governors that no assistance was given to or received by him during the examination.]

[(e)] Pursuant to the Rule 9600 Series, [the Association] NASD may, in exceptional cases and where good cause is shown, waive the applicable Qualification Examination and accept other standards as evidence of an applicant's qualifications for registration. Advanced age[,] or physical infirmity [or experience in fields ancillary to the investment banking or securities business] will not individually of themselves constitute sufficient grounds to waive a Qualification Examination. Experience in fields ancillary to the investment banking or securities business may constitute sufficient grounds to waive a Qualification Examination.

(f) Renumbered as (e)

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1080. Confidentiality of Examinations

[The Association] NASD considers all of its Qualification Examinations to be highly confidential. The removal from an examination center, reproduction, disclosure, receipt from or passing to any person, or use for study purposes of any portion of such Qualification Examination, whether of a present or past series, or any other use which would compromise the effectiveness of the Examinations and the use in any manner and at any time of the questions or answers to the Examinations are prohibited and are deemed to be a violation of Rule 2110. An applicant cannot receive assistance while taking the examination. Each applicant shall certify to the Board that no assistance was given to or received by him during the examination.

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1100. Foreign Associates

(a) No Change.

(b) Prior to the time the exemption provided for in paragraph (a) hereof may become effective, the member desiring to employ any such person must file with [the Association] NASD a [form designated "Application for Classification as a Foreign Associate"] "Uniform Application for Securities Industry Registration or Transfer" for each such person and must certify that such person meets the criteria of paragraph (a), as well as that:

(1) through (2) No Change.

(c) No Change.

[1110. Registration of Government Securities Principals and Representatives]

[1111. Registration of Principals]

[All persons associated with a member not previously registered as a principal who are to function as government securities principals shall be registered as such with the Association.]

[(a) Definition of Government Securities Principal]

[Persons associated with a member who are:]

[(1) engaged in the management or supervision of the member's government securities business, including:]

[(A) underwriting, trading or sales of government securities;]

[(B) financial advisory or consultant services for issuers in connection with the issuance of government securities;]

[(C) research or investment advice, other than general economic information or advice, with respect to government securities in connection with the activities described in (A) and (B) above;]

[(D) activities other than those specifically mentioned that involve communication, directly or indirectly, with public investors in government securities in connection with the activities described in (A) and (B) above; or]

[(2) are responsible for supervision of:]

[(A) the processing and clearance activities with respect to government securities; or]

[(B) the maintenance of records involving any of the activities described in paragraph (a)(1) above;]

[are designated as principals.]

[(b) Notification of Principal Status]

[A member shall promptly notify the Association of the assumption by an individual not previously registered with the member as a principal on the form designated by the Board of Governors accompanied by the applicable fees.]

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[1113. Persons Exempt from Registration]

Persons associated with a member whose functions are exclusively clerical or ministerial are not required to register with the Association.]