

INFORMATIONAL

Exempted Securities

SEC Approves New Rule Relating To The Application Of NASD Rules And Interpretive Materials To Exempted Securities

SUGGESTED ROUTING

The Suggested Routing function is meant to aid the reader of this document. Each NASD member firm should consider the appropriate distribution in the context of its own organizational structure.

- Executive Representatives
- Legal & Compliance
- Registered Representatives
- Senior Management

KEY TOPICS

- Exempted Securities
- Government Securities
- Group Variable Contracts
- Non-Cash Compensation

Executive Summary

On July 31, 2001, the Securities and Exchange Commission (SEC) approved National Association of Securities Dealers, Inc. (NASD®) Rule 0116, which enumerates those NASD rules and interpretive materials that apply to transactions and business activities involving exempted securities, other than municipal securities.¹ The rule change also codifies an NASD staff interpretation that the non-cash compensation provisions set forth in paragraph (g) of NASD Rule 2820 apply to group variable contracts that are exempted securities.

The text of Rule 0116 is provided in Attachment A. This rule becomes effective on **October 28, 2001**.

Questions/Further Information

Questions concerning this Notice may be directed to the Office of General Counsel, NASD Regulation, Inc., at (202) 728-8071.

Background And Discussion

Through the passage of the Government Securities Act Amendments of 1993 (GSAA), Congress authorized the NASD to apply its sales practice rules to transactions involving exempted securities, other than municipal securities. In 1996, the SEC approved an NASD proposal to implement its new authority granted under the GSAA.² The 1996 SEC Order set forth the NASD rules and interpretive materials that apply to transactions involving exempted securities,

except municipal securities. In addition, in *Notice to Members (NtM) 96-66* (October 1996), the NASD also enumerated the NASD rules and interpretive materials that are applicable to transactions in exempted securities, excluding municipal securities.³

Although *NtM 96-66* listed the NASD rules and interpretive materials outlined in the 1996 SEC Order, the *NASD Manual* did not identify them. New Rule 0116 now codifies the rules and interpretive materials that are applicable to transactions in exempted securities (other than municipal securities) as outlined in the 1996 SEC Order and *NtM 96-66*.⁴ The new rule will help members, their associated persons, and other interested persons identify those NASD rules and interpretive materials applicable to transactions involving certain exempted securities.

In addition, new Rule 0116 codifies an NASD staff interpretation concerning the application of Rule 2820(g) (non-cash compensation provision) to certain group variable contracts that are exempted securities.⁵ When the NASD identified the NASD rules that would apply to exempted securities following the passage of the GSAA, it had not adopted NASD Rule 2820(g), and thus Rule 2820(g) was not included in the 1996 SEC Order and *NtM 96-66*. However, since the implementation of Rule 2820(g), the staff consistently has interpreted Rule 2820(g) to apply to group variable contracts that are exempted securities.

Endnotes

- 1 See Securities Exchange Act Release No. 44631 (July 31, 2001), 66 FR 41283 (August 7, 2001) (order approving File No. SR-NASD-00-38) (the "SEC Approval Order").
- 2 See Securities Exchange Act Release No. 37588 (August 20, 1996), 61 FR 44100 (August 27, 1996) (order approving File No. SR-NASD-95-39) (the "1996 SEC Order").
- 3 NASD rules and interpretive materials in the Rule 8000 Series were omitted from the list in *NtM* 96-66, although they were included in the 1996 SEC Order.
- 4 Rule 0116(b) provides that, unless stated otherwise, members and their associated persons engaging in transactions and business activities relating to exempted securities, other than municipal securities, are subject to the following NASD Rules and Interpretive Materials: 2110, 2120, 2210, IM-2210-1, IM-2210-2, IM-2210-3, 2250, 2270, 2310, IM-2310-2, IM-2310-3, 2320, 2330, IM-2330, 2340, 2430, 2450, 2510, 2520, 2521, 2522, IM-2522, 2770, 2780, 2820(g), 2910, 3010, 3020, 3030, 3040, 3050, 3060, 3070, 3110, IM-3110, 3120, 3130, IM-3130, 3131, 3140, 3230, 3310, IM-3310, 3320, IM-3320, 3330, 8110, 8120, 8210, 8221, 8222, 8223, 8224, 8225, 8226, 8227, 8310, IM-8310-1, IM-8310-2, 8320 and 8330. This list reflects any deletions or other revisions to the rules and interpretive materials originally enumerated in the 1996 SEC Order. A detailed discussion of these changes is provided in the SEC Approval Order.
- 5 Rule 2820(g) limits the manner in which members and their associated persons may pay or accept non-cash compensation in connection with the sale or distribution of variable contracts.

© 2001, National Association of Securities Dealers, Inc. (NASD). All rights reserved. Notices to Members attempt to present information to readers in a format that is easily understandable. However, please be aware that, in case of any misunderstanding, the rule language prevails.

ATTACHMENT A – RULE TEXT

Note: All language is new.

0116. Application of Rules of the Association to Exempted Securities

(a) For purposes of this Rule, the terms “exempted securities” and “municipal securities” shall have the meanings specified in Sections 3(a)(12) and 3(a)(29) of the Act, respectively.

(b) Unless otherwise indicated within a particular provision, the following Rules of the Association and Interpretive Materials thereunder are applicable to transactions and business activities relating to exempted securities, except municipal securities, conducted by members and associated persons: 2110, 2120, 2210, IM-2210-1, IM-2210-2, IM-2210-3, 2250, 2270, 2310, IM-2310-2, IM-2310-3, 2320, 2330, IM-2330, 2340, 2430, 2450, 2510, 2520, 2521, 2522, IM-2522, 2770, 2780, 2820(g), 2910, 3010, 3020, 3030, 3040, 3050, 3060, 3070, 3110, IM-3110, 3120, 3130, IM-3130, 3131, 3140, 3230, 3310, IM-3310, 3320, IM-3320, 3330, 8110, 8120, 8210, 8221, 8222, 8223, 8224, 8225, 8226, 8227, 8310, IM-8310-1, IM-8310-2, 8320 and 8330.