

# Notice to Members

OCTOBER 2005

## SUGGESTED ROUTING

Legal & Compliance  
Registered Representatives  
Senior Management

GUIDANCE

## Minor Rule Violation Plan

SEC approves NASD Interpretive Material to Rule 9216 regarding NASD's MRVP; **Effective Date: November 14, 2005**

## KEY TOPICS

IM-9216  
Rule 9216(b)  
Minor Rule Violation Plan (MRVP)

## Executive Summary

On August 18, 2005, the Securities and Exchange Commission (SEC) approved amendments to NASD Interpretive Material 9216-2 (IM-9216-2), regarding NASD's MRVP.<sup>1</sup> The new rule text is contained in Attachment A and is effective on November 14, 2005.

## Questions/Further Information

Questions concerning this *Notice* may be directed to Shirley H. Weiss, Associate General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8844.

## Background

In 1984, the SEC adopted amendments to Rule 19d-1(c) under the Securities Exchange Act of 1934 to allow self-regulatory organizations to adopt, with SEC approval, plans for the disposition of minor violations of rules. In 1993, pursuant to SEC Rule 19d-1(c), NASD established an MRVP. The rules governing NASD's MRVP may be found in NASD Rule 9216(b).<sup>2</sup> Rule 9216(b) authorizes NASD to impose a fine of \$2,500 or less on any member or associated person of a member for a violation of any of the rules specified in IM-9216.<sup>3</sup> 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.

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The purpose of the MRVP is to provide for a meaningful sanction for the 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. 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.

## Discussion

NASD has amended its MRVP as follows:

**—Rules 4632, 4642, 4652, 4632A, 5430, 6130, 6170, 6130A, 6170A, 6230, 6420, 6550, 6620, and 6720—Transaction reporting in debt and equity securities.**

NASD has combined in one entry all of the rule violations eligible for disposition under the MRVP that relate to transaction reporting and audit trail requirements in equity and debt securities. This entry includes violations of transaction reporting and audit trail requirements related to (1) the NASDAQ Market Center; (2) NASD's Trade Reporting and Comparison Service (TRACS);<sup>4</sup> and (3) the Trade Reporting and Compliance Engine (TRACE).

To effectuate this, NASD has eliminated the separate minor rule violation pertaining to Rules 6130 and 6170 and has added those rules to this entry. NASD has also added to the MRVP, and this entry, violations of Rules 4632A, 5430, 6130A and 6170A, which relate to TRACS requirements.<sup>5</sup> Including violations of the ADF transaction-reporting requirements in the MRVP is consistent with the current minor rule violations for transaction reporting in equity securities.

NASD has also eliminated the reference in the MRVP to a violation of the Fixed Income Pricing System (FIPS), and replaced it with a violation of Rule 6230, the TRACE transaction-reporting rule.<sup>6</sup> In adopting the TRACE rules in 2001, NASD eliminated FIPS, which required members to report trades for 50 high-yield debt securities. Since the TRACE system replaced and expanded upon FIPS, NASD has amended the MRVP to replace the FIPS violation with a violation of the TRACE system transaction-reporting requirement.

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**—Rules 2210, 2211, and 2220, and IM-2210-1, -2210-2, -2210-3, -2210-4, -2210-5, -2210-7, and -2210-8—Communications with the public.**

NASD's advertising rules (Rules 2210, 2211, and 2220, and related Interpretive Materials) contain general and specific standards applicable to all member communications with the public. These standards prohibit incomplete, unbalanced, or unfair communications as well as exaggerated, unwarranted, or misleading statements or claims. The rules also enumerate specific standards for certain types of communications, including recommendations, hedge clauses and projections. In addition, the rules set forth standards for the use and disclosure of the member's name.

Prior to the adoption of these amendments, NASD could issue minor rule violations only for procedural violations of the advertising rules, such as a failure to have advertisements and sales literature approved by a principal prior to use or a failure to meet specified time limits for filing advertisements. It was NASD's experience, however, that, based on the facts and circumstances, certain content-related violations of these rules could warrant more than a Letter of Caution, yet not rise to a level requiring or meriting full disciplinary action. Accordingly, as amended, the MRVP provision concerning communications with the public allows NASD to address these minor or technical violations of content-related advertising rules, which might include, for example only, a technical violation of the provisions on the use and disclosure of members' names.

**—Failure to provide or update contact information as required by NASD Rules.**

NASD has expanded the MRVP to include, as a general category, a member's failure to identify to NASD and keep current information regarding any contact person that a member must provide to NASD under any current or future NASD rule. For example, a member's failure to provide or update emergency contact information under Rule 3520 or failure to provide or update its executive representative designation and contact information as required by Rule 1150 would be eligible for disposition as a minor rule violation under this category.<sup>7</sup>

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## Endnotes

- 1 Exchange Act Rel. No. 52294 (Aug. 18, 2005), 70 FR 49700 (Aug. 24, 2005) (SR-NASD-2004-025).
- 2 See Exchange Act Rel. No. 32383 (May 28, 1993), 58 FR 31768 (June 4, 1993) (SR-NASD-93-6); see also *Notice to Members* 93-42 (July 1993).
- 3 In 2001, the SEC approved significant amendments to NASD's MRVP. In addition, in 2004, the SEC approved an amendment to NASD's MRVP to include failure to timely submit amendments to the Form U5 (Uniform Termination Notice for Securities Industry Registration).
- 4 TRACS is the trade reporting system for NASD's Alternative Display Facility (ADF).
- 5 NASD notes that Rule 5430 governs both TRACS and the NASDAQ Market Center transaction reporting requirements.
- 6 Prior to July 1, 2002, the Rule 6200 Series pertained to FIPS, and Rule 6240 governed transaction reporting in high yield fixed income securities.
- 7 See also Rule 1120(a)(7) (requirement to provide continuing education regulatory element contact person). NASD notes that it generally has sought to achieve consistency regarding the frequency in which members must review and update contact information (namely, within 17 business days after the end of each calendar quarter, which is consistent with the schedule for filing the quarterly FOCUS report).

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## **ATTACHMENT A**

New language is underlined; deletions are in brackets.

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### **9200. DISCIPLINARY PROCEEDINGS**

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#### **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.]

—Rules 2210, 2211, and 2220, and IM-2210-1, -2210-2, -2210-3, -2210-4, -2210-5, -2210-7, and -2210-8—Communications with the public.

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

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

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

—Article IV of the NASD By-Laws—Failure to timely submit amendments to Form BD.

—Article V of the NASD By-Laws —Failure to timely submit amendments to Form U4.

—Article V of the NASD By-Laws —Failure to timely submit amendments to Form U5.

—Rule 1120—Failure to comply with the Firm Element of the continuing education requirements.

—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.

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- Rules 4632, 4642, 4652, 4632A, 5430, 6130, 6170, 6130A, 6170A, 6230[6240], 6420, 6550, 6620, and 6720—Transaction reporting in debt and equity[, convertible debt, and high yield] securities.
  - [—Rules 6130 and 6170—Transaction reporting to the Automatic Confirmation Transaction Service (“ACT”).]
  - Rules 6954 and 6955—Failure to submit data in accordance with the Order Audit Trail System (“OATS”).
  - Rule 11870—Failure to abide by Customer Account Transfer Contracts.
  - Failure to provide or update contact information as required by NASD Rules.
  - SEC Exchange Act Rule 11Ac1-4—Failure to properly display limit orders.
  - SEC Exchange Act Rule 11Ac1-1(c)(5)—Failure to properly update published quotations in certain Electronic Communication Networks (“ECN[‘]s”).
  - 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 timely 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.

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