

Notice to Members

FEBRUARY 2006

SUGGESTED ROUTING

Continuing Education
Executive Representatives
Legal & Compliance
Operations
Registration
Senior Management
Training

KEY TOPICS

Active Military Duty
Continuing Education
IM-1000-2
Inactive Status
Registration Requirements
Rule 1021(c)
Rule 1031(c)
Rule 1041(c)
Transaction-Related Compensation

GUIDANCE

Active Military Service

Amendments Relating to the Status of Persons Serving in the Armed Forces of the United States; **Effective Dates: IM-1000-2(a) and IM-1000-2(b): November 15, 2005; IM-1000-2(c): March 27, 2006**

Executive Summary

On November 15, 2005, NASD filed with the Securities and Exchange Commission (SEC) for immediate effectiveness amendments to Interpretive Material (IM) 1000-2 to (1) clarify that the scope of the relief provided in the IM extends to any registered person of a firm who volunteers for or is called into active military duty, not just registered representatives; (2) codify the staff's existing interpretation with respect to the receipt of transaction-related compensation by registered persons who volunteer for or are called into active military duty; (3) clarify that the relief provided to a registered person of a firm who volunteers for or is called into active military duty is available to the person during the period that such person remains registered with the firm, regardless of whether the person returns to employment at a different firm upon completion of his or her active military duty; and (4) clarify that the "inactive" status designation is available to registered persons and sole proprietors who volunteer for or are called into active duty in the Armed Forces of the United States and is available to them only while they remain on active military duty.¹ As part of these amendments, NASD also labeled and numbered the existing rule text. These amendments became effective on November 15, 2005.

Additionally, on January 26, 2006, the SEC approved amendments to IM-1000-2 to toll the two-year expiration provisions for qualification examination requirements set forth in Rules 1021(c), 1031(c), and 1041(c) for certain former registered persons serving in the Armed Forces of the United States, including persons who commence their

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active military duty within two years after they have ceased to be registered with a member and persons who terminate their registration with a member while on active military duty.² These amendments become effective on March 27, 2006.

IM-1000-2, as amended, is set forth in Attachment A.

Questions/Further Information

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

Background and Discussion

IM-1000-2 permits a firm to place a registered representative on “inactive” status while serving in the Armed Forces of the United States. Such “inactive” status excuses a registered representative from continuing education obligations, waives dues and assessments, and ensures that he or she is not subject to the two-year expiration period for securities licenses of persons who cease to be registered with a member (two-year licensing expiration provisions).³

Historically, NASD has provided tailored regulatory relief to securities industry professionals who volunteer for or are called into active military duty. For instance, following the September 11, 2001 attacks, NASD filed with the SEC for immediate effectiveness a rule change that amended IM-1000-2 to codify the staff’s position regarding the relief from Rule 1120 (Continuing Education Requirements) for securities industry professionals who volunteer for or are called into active military duty.⁴ Additionally, following discussions with SEC staff, NASD published on its Web site guidance stating that “inactive” registered persons serving in the Armed Forces of the United States may receive transaction-related compensation, provided that they do not perform any functions of a registered person while on “inactive” status.⁵

NASD recently received requests for further clarification on the scope of IM-1000-2 and the accompanying guidance. In particular, members questioned whether the IM applies to registered persons other than registered representatives and whether registered persons can receive commissions on accounts that have been temporarily re-assigned in their absence. Members also questioned the manner in which the relief applies if a registered person seeks employment with a different member upon completing active military duty.⁶ Members further requested that NASD toll the two-year licensing expiration provisions in certain cases, such as where a person commences active military duty within two years after he or she has ceased to be registered with a member or where a person on active military duty ceases to be registered with a member, but seeks employment in the industry following completion of active service.

In response, NASD has amended IM-1000-2 as described in the following pages.

IM-1000-2(a) (Inactive Status of Currently Registered Persons) and IM-1000-2(b) (Inactive Status of Sole Proprietorships)

NASD has amended IM-1000-2 to clarify that the scope of the relief provided in the IM extends to any registered person of a member who volunteers for or is called into active military duty, not just registered representatives.

NASD also has amended IM-1000-2 to expressly state that a registered person of a member who volunteers for or is called into active duty in the Armed Forces of the United States and who is placed on “inactive” status will remain eligible to receive transaction-related compensation, including continuing commissions, because he or she remains registered with a member of NASD. In addition, NASD has amended IM-1000-2 to provide that an employing member may allow such a person to enter into an arrangement with another registered person of the member to take over and service the person’s accounts and to share transaction-related compensation based upon the business generated by such accounts. NASD further has amended IM-1000-2 to state that such “inactive” persons may not perform any of the duties performed by a registered person. These amendments are consistent with NASD’s existing interpretation with respect to the receipt of transaction-related compensation by registered persons actively serving in the Armed Forces of the United States.⁷

Additionally, NASD has amended IM-1000-2 to clarify that the relief provided to a registered person of a member who volunteers for or is called into active military duty is available to the person during the period that such person remains registered with the member, regardless of whether the person returns to employment at a different member upon completion of his or her active military duty. NASD will not rescind the relief provided to such a person simply because he or she decides to register with another member upon completion of his or her active military duty. For instance, if a registered person of Firm Y who volunteers for or is called into active military duty and who is placed on “inactive” status with Firm Y decides to register with Firm Z upon completion of her active military duty, NASD will not invalidate the relief that was provided to the person while on “inactive” status with Firm Y.

Moreover, NASD has amended IM-1000-2 to clarify that the “inactive” status designation is available to registered persons and sole proprietors who volunteer for or are called into active duty in the Armed Forces of the United States and is available to them only while they remain on active military duty. Therefore, a registered person who is placed on “inactive” status pursuant to IM-1000-2 will be removed from “inactive” status if the person ceases to be registered with a member while serving in the Armed Forces of the United States. If he or she re-registers with a member while still serving in the Armed Forces of the United States, he or she will again be eligible for “inactive” status pursuant to the IM. Likewise, a registered person or sole proprietor who is placed on “inactive” status pursuant to IM-1000-2 will be removed from “inactive” status if the registered person or sole proprietor is no longer on active military duty.

Effective Date

IM-1000-2(a) and IM-1000-2(b) became effective on November 15, 2005.

Notifying NASD

With respect to a person seeking relief pursuant to IM-1000-2(a) or IM-1000-2(b), the firm with which the person is registered or the sole proprietor must provide to NASD the following documentation regarding the person's active military service start date once the person's military service starts:

1. A copy of the individual's orders (official call-up notification) or a copy of the letter of leave request for individuals that voluntarily join (either document must include the individual's start date, and should include the individual's military branch and location of service duty); and
2. A letter from the firm (on firm letterhead) to NASD that includes the firm's CRD number, date that the individual started active military service, individual's name and individual's CRD number.

Additionally, the firm with which the person is registered or the sole proprietor should provide to NASD the following documentation regarding the person's active military service end date once the person's military service ends:

1. A copy of the individual's discharge papers that indicate the start and end dates of service; and
2. A letter from the firm to NASD that includes the firm's CRD number, date the individual returned to the firm, individual's name and individual's CRD number.

IM-1000-2(c) (Status of Formerly Registered Persons)

NASD also has amended IM-1000-2 to toll the "two-year licensing expiration provisions" for a person previously registered with a member who commences his or her active military duty within two years after he or she has ceased to be registered with the member. The tolling period will start on the date such person enters active military service and will terminate 90 days following the person's completion of active service in the Armed Forces of the United States. The amendment requires that NASD be properly notified (as described below) of the person's period of active military service within 90 days following his or her completion of active service or upon his or her re-registration with a member, whichever occurs first. If such person does not re-register with a member within 90 days following his or her completion of active service in the Armed Forces of the United States, the amount of time in which the person must become re-registered with a member without being subject to the "two-year licensing expiration provisions" will consist of the standard two-year period reduced by the period of time between the person's termination of registration and beginning of active service in the Armed Forces of the United States.⁸

Finally, NASD has amended IM-1000-2 to toll the “two-year licensing expiration provisions” for a person placed upon “inactive” status pursuant to IM-1000-2 who while serving in the Armed Forces of the United States ceases to be registered with a member. In such cases, the tolling period will start on the date such person ceases to be registered with the member and will terminate 90 days following the person’s completion of active service in the Armed Forces of the United States, and NASD has to be properly notified of the person’s period of active military service within two years following his or her completion of active service or upon his or her re-registration with a member, whichever occurs first. NASD will toll the “two-year licensing expiration provisions” for such persons based on available information in the Central Registration Depository (CRD) regarding their active military status. If such person does not re-register with a member within 90 days following his or her completion of active service in the Armed Forces of the United States, the person would have 90 days plus two years following the end of the person’s active service in the Armed Forces of the United States to become re-registered with a member.⁹

Effective Date

IM-1000-2(c) becomes effective on March 27, 2006.

Notifying NASD

With respect to a person seeking relief pursuant to IM-1000-2(c), the firm with which the person is seeking to register must provide to NASD the following documentation:

1. After the firm has submitted a Form U4, a letter from the firm to NASD notifying NASD that the individual was on active military duty. The letter should also include the firm’s CRD number, individual’s name, individual’s CRD number, and the date that the firm submitted the Form U4; and
2. A copy of the individual’s discharge papers that indicate the start and end dates of active military service.

Submitting Documentation

The documentation required by IM-1000-2 must be submitted to NASD by facsimile or mail:

Fax Number: (240) 386-4849

Mailing Address: NASD
Registration & Disclosure Department
P.O. Box 9495
Gaithersburg, MD 20898-9495

Endnotes

- 1 See Securities Exchange Act Release No. 52980 (December 19, 2005), 70 FR 76477 (December 27, 2005) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to the Status of Registered Persons and Sole Proprietors Serving in the Armed Forces of the United States; File No. SR-NASD-2005-134).
- 2 See Securities Exchange Act Release No. 53182 (January 26, 2006), 71 FR 5391 (February 1, 2006) (Order Approving a Proposed Rule Change Relating to the Status of Former Registered Persons Serving in the Armed Forces of the United States; File No. SR-NASD-2005-135).
- 3 NASD Rules 1021(c), 1031(c), and 1041(c) provide that if a person does not register with a member within two years of his or her last registration, his or her qualification as a principal, representative or assistant representative will lapse and the person must then retest to function as a principal, representative or assistant representative. In the case of a person on "inactive" status due to active military duty, because he or she is considered registered for purposes of NASD Rules, the "two-year licensing expiration provisions" do not apply.
- 4 See Securities Exchange Act Release No. 45259 (January 9, 2002), 67 FR 2256 (January 16, 2002) (Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Relieve Registered Representatives Serving in the Armed Forces From Continuing Education Requirements; File No. SR-NASD-2002-03).
- 5 See *Registered Persons on Active Military Duty* (available at: www.nasd.com/RegisteredMilitary).
- 6 Some members questioned whether the return of a registered person who volunteers for or is called into active military duty to employment at a different member would negate or invalidate the relief the person has received while being deemed "inactive" at their original employing member.
- 7 The NASD staff's interpretation with respect to the receipt of transaction-related compensation by registered persons serving in the Armed Forces of the United States also is consistent with the New York Stock Exchange, Inc.'s (NYSE) interpretation to NYSE Rule 345(a), which the NYSE codified in June 2002. See NYSE Interpretation Handbook, NYSE Rule 345(a)/03. Firms should be aware that the relief regarding the ongoing receipt of transaction-based compensation does not extend to a sole proprietor member placed on "inactive" status pursuant to IM-1000-2. Rather, consistent with current practice, NASD staff, in consultation with SEC staff, will address such issues in the context of a sole proprietor member placed on "inactive" status on a case-by-case basis.
- 8 For instance, if a person terminates his registration with a firm on August 1, 2005 is called into active military duty on November 1, 2005 and returns from active military duty on May 1, 2006, NASD would toll the "two-year licensing expiration provisions" beginning on November 1, 2005 until July 30, 2006 (which is 90 days following completion of his active military duty). In this example, NASD would have to be notified of his period of active military service by no later than July 30, 2006 or upon his re-registration with a member, whichever occurs first. Further, if he does not re-register with a member by July 30, 2006, he would then have 21 months remaining (24 months less the three months that ran prior to his entering active service) to re-register with a firm without having to re-take a qualification exam or seek a waiver.

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- 9 For example, assume a person registered with Firm A, enters active military duty on January 1, 2006, and is placed on "inactive" status for purposes of NASD registration. He then terminates his registration with Firm A on July 1, 2006 while still on active military duty. He returns from active military duty on December 1, 2006. In this example, NASD would remove his "inactive" status designation on July 1, 2006 because he has ceased to be registered with a member. However, NASD would toll the "two-year licensing expiration provisions" beginning on July 1, 2006, until March 1, 2007 (which is 90 days following completion of his active military duty). NASD would have to be notified of his period of active military service by no later than December 1, 2008 (which is two years following completion of his active military duty) or upon his re-registration with a member, whichever occurs first.

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ATTACHMENT A

New language is underlined; deleted language is in brackets.

IM-1000-2. Status of [Sole Proprietors and Registered Representatives] Persons Serving in the Armed Forces of the United States

(a) Inactive Status of Currently Registered Persons

(1) A[ny] [R]registered [Representative] person of a member who volunteers for or is called into active duty in the Armed Forces of the United States shall be placed, after proper notification to [the Executive Office] NASD, upon inactive status and need not be re-registered by such member upon his or her return to active employment with the member. Such a person will remain eligible to receive transaction-related compensation, including continuing commissions, because he or she remains registered with a member of NASD. The employing member also may allow such a person to enter into an arrangement with another registered person of the member to take over and service the person's accounts and to share transaction-related compensation based upon the business generated by such accounts. However, since such persons are inactive, they may not perform any of the duties performed by a registered person.

[Any member (Sole Proprietor) who temporarily closes his or her business by reason of volunteering or being called into the Armed Forces of the United States, shall be placed, after proper notification to the Executive Office, on inactive status until his or her return to active participation in the investment banking and securities business.]

(2) A [R]registered [Representative] person who is placed on inactive status [as set forth above] pursuant to this paragraph (a) shall not be included within the definition of "Personnel" for purposes of the dues or assessments as provided in Article VI of the NASD By-Laws.

[Any member placed on inactive status as set forth above shall not be required to pay dues or assessments during the pendency of such inactive status and shall not be required to pay an admission fee upon return to active participation in the investment banking and securities business.]

(3) A [R]registered [Representative] person who is placed on inactive status [as set forth above] pursuant to this paragraph (a) shall not be required to complete either of the Regulatory or Firm Elements of the continuing education requirements set forth in Rule 1120 during the pendency of such inactive status.

(4) The relief provided in subparagraphs (a)(1), (a)(2), and (a)(3) shall be available to a registered person who is placed on inactive status pursuant to this paragraph (a) during the period that such a person remains registered with the member with which he or she was registered at the beginning of active duty in the Armed Forces of the United States, regardless of whether the person returns to active employment with another member upon completion of his or her active duty in the Armed Forces of the United States.

(5) The relief described in this paragraph (a) will be provided only to a person registered with a member and only while the person remains on active military duty.

(b) Inactive Status of Sole Proprietorships

(1) A member that is a sole proprietor who temporarily closes his or her business by reason of volunteering for or being called into active duty in the Armed Forces of the United States, shall be placed, after proper notification to NASD, on inactive status while the member remains on active military duty.

(2) A sole proprietor member placed on inactive status as set forth in this paragraph (b) shall not be required to pay dues or assessments during the pendency of such inactive status and shall not be required to pay an admission fee upon return to active participation in the investment banking and securities business.

(3) The relief described in this paragraph (b) will be provided only to a sole proprietor member and only while the person remains on active military duty.

(c) Status of Formerly Registered Persons

(1) If a person who is currently not registered with a member volunteers for or is called into active duty in the Armed Forces of the United States at any time within two years after the date the person ceases to be registered with a member, NASD will defer the lapse of registration requirements set forth in Rules 1021(c), 1031(c), and 1041(c) (i.e., toll the two-year expiration provisions for qualification examination requirements). NASD will defer the lapse of registration requirements commencing on the date the person begins actively serving in the Armed Forces of the United States, provided that NASD is properly notified of the person's period of active military service within 90 days following his or her completion of active service or upon his or her re-registration with a member, whichever occurs first. The deferral will terminate 90 days following the person's completion of active service in the Armed Forces of the United States. Accordingly, if such person does not re-register with a member within 90 days following his or her completion of active service in the Armed Forces of the United States, the amount of time in which the person must become re-registered with a member without being subject to the qualification examination requirements shall consist of the standard two-year period provided in Rules 1021(c), 1031(c), and 1041(c) reduced by the period of time between the person's termination of registration and beginning of active service in the Armed Forces of the United States.

(2) If a person placed upon inactive status while serving in the Armed Forces of the United States ceases to be registered with a member, NASD will defer the lapse of registration requirements set forth in Rules 1021(c), 1031(c), and 1041(c) (i.e., toll the two-year expiration provisions for qualification examination requirements) during the pendency of his or her active service in the Armed Forces of the United States. NASD will defer the lapse of registration requirements based on existing information in the Central Registration Depository, provided that NASD is properly notified of the person's period of active military service within two years following his or her completion of active service or upon his or her re-registration with a member, whichever occurs first. The deferral will terminate 90 days following the person's completion of active service in the Armed Forces of the United States. Accordingly, if such person does not re-register with a member within 90 days following his or her completion of active service in the Armed Forces of the United States, the amount of time in which the person must become re-registered with a member without being subject to the qualification examination requirements shall consist of the standard two-year period provided in Rules 1021(c), 1031(c), and 1041(c).