

November 26, 2002

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-2002-171 – Amendment 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 Brian J. Woldow, Office of General Counsel, Regulatory Policy and Oversight, NASD, at (202) 728-6927; e-mail brian.woldow@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Barbara Z. Sweeney
Senior Vice President
and Corporate Secretary

Enclosures

File No. SR-NASD-2002-171
Consists of 15 Pages
November 26, 2002

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 ("Exchange Act"), 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) (Violations Appropriate for Disposition Under the Plan Pursuant to SEC Rule 19d-1(c)(2)) to clarify that a failure to timely file annual audit reports is eligible for disposition under NASD's Minor Rule Violation Plan ("MRVP" or "the Plan"). Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

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

—Rules 2210(b) and (c) and Rules 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.

—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.

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

—Rule 3010(b)(2)(vii)—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.

—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 proposed rule change was approved by the Board of Directors of NASD Regulation, Inc. at its meeting on March 29, 2000, which authorized the filing of the rule change with the SEC. Counsel for The Nasdaq Stock Market and NASD Dispute Resolution were 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 reviewed the proposed rule change at its meeting on March 30, 2000. 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 adopt amendments to NASD interpretative materials without recourse to the membership for approval.

(b) Questions regarding this rule filing may be directed to Brian J. Woldow, Attorney, Office of General Counsel, Regulatory Policy and Oversight, NASD, at (202) 728-6927.

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

(a) Purpose

The purpose of this proposed rule change is to clarify that a failure to timely file annual audit reports is appropriate for disposition under NASD's MRVP. As described in more detail herein, NASD believes that the current rule language in IM-9216 referring to SEC Exchange Act Rule 17a-5 does not clearly reflect that a failure to timely file annual audit reports is included in NASD's MRVP.

NASD's Minor Rule Violation Plan

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.¹ In 1993, pursuant to SEC Rule 19d-1(c), NASD established a MRVP.² See NASD Rule 9216(b). In 2001, the SEC approved amendments to NASD's MRVP.³

NASD 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 NASD IM-9216. The number and seriousness of the violations, as well as the previous disciplinary history of the respondent is reviewed to determine if a matter is appropriate for disposition under the Plan 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.

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

¹ See Exchange Act Rel. No. 21013 (June 1, 1984), 49 Fed. Reg. 23833 (June 8, 1994).

² See Exchange Act Rel. No. 32076 (Mar. 31, 1993), 58 Fed. Reg. 18291 (Apr. 8, 1993); see also Notice to Members 93-42 (July 1993).

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

technical violation of the rule may be appropriate for disposition under the MRVP. NASD retains the discretion to bring full disciplinary proceedings.

Proposed Rule Change

As stated above, in 2001, NASD amended the MRVP to include additional violations. One of these violations is listed in IM-9216 as "SEC Exchange Act Rule 17a-5—failure to timely file FOCUS reports." In the Notice of Filing of Proposed Rule Change, the SEC, referring to language in the NASD 19b-4 rule filing, stated that NASD "proposes to institute minor rule violations for failure of a member to timely file monthly, quarterly, and annual reports required by SEC Rule 17a-5, also known as FOCUS reports."⁴ SEC Rule 17a-5 requires that firms file both FOCUS reports and annual audit reports; however, for purposes of NASD's MRVP, an annual audit report currently is defined as being included in the term "FOCUS reports." As a result, NASD believes that the MRVP may not clearly reflect that a failure to timely file annual audit reports, as well as FOCUS reports, under SEC Rule 17a-5 is proper for disposition as a minor rule violation. NASD therefore is proposing this rule change to clarify that a failure to timely file annual audit reports is encompassed within the MRVP.

(b) Statutory Basis

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's 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 this

⁴ Exchange Act Rel. No. 43330 (Sept. 22, 2000), 65 Fed. Reg. 58585 (Sept. 29, 2000). This statement is also repeated in *Notice to Members* 01-54 (Aug. 2001), which announced the SEC approval order.

proposed rule change is necessary to clarify that a failure to timely file annual audit reports is included in NASD's MRVP.

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

Written comments were neither solicited nor received.

6. Extension of Time Period for Commission Action

Not applicable.

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

The proposed rule change is effective upon filing pursuant to Section 19(b)(3)(A) of the Act and paragraph (f)(6) of Rule 19b-4 thereunder, in that the proposed rule change does not significantly affect the protection of investors or the public interest and does not impose any significant burden on competition. In accordance with Rule 19b-4(f)(6)(iii), NASD submitted written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change prior to the date of filing. In that notice of intent, NASD requested that the Commission waive the requirement that the rule change, by its terms, not become operative for 30 days after the date of the filing as set forth in Rule 19b-4(f)(6)(iii), as consistent with the protection of investors and the public interest. The Commission agreed to waive that

requirement. Therefore, the proposed rule change is effective upon filing pursuant to Section 19(b)(3)(A) of the Exchange Act and Rule 19b-4(f)(6) thereunder.

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

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, INC.

BY: _____
Barbara Z. Sweeney, Senior Vice President and
Corporate Secretary

Date: November 26, 2002

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- [] ; File No. SR-NASD-2002-169)

Self-Regulatory Organizations; Notice of and Immediate Effectiveness of Proposed Rule Change
by National Association of Securities Dealers, Inc. Relating 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 November 19, 2002, 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. NASD has designated the proposed rule change as constituting a "non-controversial" rule change under paragraph (f)(6) of Rule 19b-4 under the Act,³ which renders the proposal effective upon receipt of this filing by the Commission. 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 proposing to amend Interpretative Material 9216 (IM-9216) to clarify that a failure to timely file annual audit reports is eligible for disposition under NASD's Minor Rule Violation Plan ("MRVP" or the "Plan"). Below is the text of the proposed rule change. Proposed new language is in italics; proposed deletions are in brackets.

¹ 15 U.S.C. § 78s(b)(1).

² 17 CFR § 240.19b-4.

³ 17 CFR § 240.19b-4.

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

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

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—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.

* * * * *

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

The purpose of this proposed rule change is to clarify that a failure to timely file annual audit reports is appropriate for disposition under NASD's MRVP. As described in more detail herein, NASD believes that the current rule language in IM-9216 referring to SEC Exchange Act Rule 17a-5 does not clearly reflect that a failure to timely file annual audit reports is included in NASD's MRVP.

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NASD 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 NASD IM-9216. The number and seriousness of the violations, as well as the previous disciplinary history of the respondent is reviewed to determine if a matter is appropriate for disposition under

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the Plan 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.

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. NASD retains the discretion to bring full disciplinary proceedings.

Proposed Rule Change

As stated above, in 2001, NASD amended the MRVP to include additional violations. One of these violations is listed in IM-9216 as "SEC Exchange Act Rule 17a-5—failure to timely file FOCUS reports." In the Notice of Filing of Proposed Rule Change, the SEC, referring to language in the NASD 19b-4 rule filing, stated that NASD "proposes to institute minor rule violations for failure of a member to timely file monthly, quarterly, and annual reports required by SEC Rule 17a-5, also known as FOCUS reports."⁷ SEC Rule 17a-5 requires that firms file both FOCUS reports and annual audit reports; however, for purposes of NASD's MRVP, an annual audit report currently is defined as being included in the term "FOCUS reports." As a result, NASD believes that the MRVP may not clearly reflect that a failure to timely file annual audit reports, as well as FOCUS reports, under SEC Rule 17a-5 is proper for disposition as a

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minor rule violation. NASD therefore is proposing this rule change to clarify that a failure to timely file annual audit reports is encompassed within the MRVP.

(b) Statutory Basis

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 the NASD's 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 this proposed rule change is necessary to clarify that a failure to timely file annual audit reports is included in NASD's MRVP.

(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

Written comments were neither solicited nor received.

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

The proposed rule change has been filed by the Association as a "non-controversial" rule change under Rule 19b-4(f)(6) under the Act.⁸ In accordance with Rule 19b-4(f)(6)(iii), prior to the filing date, NASD submitted written notice of its intent to file the proposed rule change along with a brief description and text of the proposed rule change. In that notice of intent, NASD

⁸ 17 CFR § 240.19b-4(f)(6).

requested that the Commission waive the requirement that the rule change, by its terms, not become operative for 30 days after the date of the filing, as consistent with the protection of investors and the public interest. The Commission agreed to waive that requirement.

Accordingly, the proposed rule change will become effective and operative upon filing pursuant to Section 19(b)(3)(A) of the Act and Rule 19b-4(f)(6) thereunder.

At any time within 60 days of this filing, the Commission may summarily abrogate this proposal if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing. 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. 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).

Jonathan G. Katz
Secretary