

September 22, 2000

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-00-58**
Transactions Involving Association and American Stock Exchange
Employees

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: Gary L. Goldsholle, Associate General Counsel, NASD Regulation Office of General Counsel, at (202) 728-8104 (e-mail gary.goldsholle@nasd.com); or Anne H. Wright, Associate Vice President and Associate General Counsel, NASD Office of General Counsel, at (202) 728-8815 (e-mail anne.wright@nasd.com). The fax number of the NASD Regulation Office of General Counsel is (202) 728-8264.

Very truly yours,

Joan C. Conley
Senior Vice President
and Corporate Secretary

Enclosures

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) under the Securities Exchange Act of 1934 (“Act”), the National Association of Securities Dealers, Inc. (“NASD”), through its wholly owned subsidiary, NASD Regulation, Inc. (“NASD Regulation”), is filing with the Securities and Exchange Commission (“SEC” or “Commission”) a proposed rule change to adopt NASD Rule 3090, to: (1) require NASD members to promptly obtain and implement a duplicate statement instruction whenever they have actual knowledge that an Association or American Stock Exchange (“Amex”) employee has a financial interest in, or controls trading in, an account; (2) prohibit NASD members from making loans to Association or Amex employees except in the context of a routine banking or brokerage relationship, or when it is clear that a personal or family relationship motivates the loan; and (3) prohibit NASD members from giving business gifts or courtesies of more than nominal value to an Association or Amex employee who has responsibility for a specific regulatory matter (*e.g.*, an examination, disciplinary proceeding, membership application, listing application, delisting proceeding, dispute-resolution proceeding) that involves the member. Below is the text of the proposed rule change. Proposed new language is underlined.

3090. Transactions Involving Association and American Stock Exchange Employees

(a) When a member has actual notice that an Association or American Stock Exchange employee has a financial interest in, or controls trading in, an account, the member shall promptly obtain and implement an instruction from the employee directing that duplicate account statements be provided by the member to the Association.

(b) No member shall directly or indirectly make any loan of money or securities to any Association or American Stock Exchange employee. Provided, however, that this prohibition does not apply to loans made in the context of disclosed, routine banking and brokerage agreements, or loans that are clearly motivated by a personal or family relationship.

(c) Notwithstanding the annual dollar limitation set forth in Conduct Rule 3060(a), no member shall directly or indirectly give, or permit to be given, anything of more than nominal value to any Association or American Stock Exchange employee who has responsibility for a regulatory matter that involves the member. For purposes of this subsection, the term "regulatory matter" includes, but is not limited to, examinations, disciplinary proceedings, membership applications, listing applications, delisting proceedings, and dispute-resolution proceedings that involve the member.

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) On January 26, 2000, the Board of Directors of NASD Regulation approved and authorized the filing of the rule change with the SEC. Pursuant to the Plan of Allocation and Delegation of Functions by the NASD to its Subsidiaries, the Nasdaq Stock Market was provided an opportunity to consult with respect to the proposed rule change. The NASD Board of Governors reviewed and ratified the proposed rule change at its meeting on January 27, 2000. No other action by the NASD is necessary for the filing of the proposed rule change. Section 1(a)(ii) of

Article VII of the NASD By-Laws permits the NASD Board of Governors to adopt NASD Rules without recourse to the membership for approval.

The NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 60 days following Commission approval. The effective date will be 30 days following publication of the Notice to Members announcing Commission approval.

(b) Questions regarding this rule filing may be directed to: Gary L. Goldsholle, Associate General Counsel, NASD Regulation Office of General Counsel, at (202) 728-8104; or Anne H. Wright, Associate Vice President and Associate General Counsel, NASD Office of General Counsel, at (202) 728-8815.

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

(a) Purpose

The NASD Code of Conduct imposes detailed ethics and conflict-of-interest requirements on Association employees (*i.e.*, employees of NASD, Inc. and all of its subsidiary and affiliated companies). The NASD is proposing a new rule, NASD Conduct Rule 3090, that will impose parallel requirements on NASD members in their dealings with Association and American Stock Exchange ("Amex") employees. The Amex, whose employees will become subject to the NASD Code of Conduct in October 2000, has filed a rule proposal (No. SR-Amex-00-23) that will make parallel changes to Amex rules.

As discussed in greater detail below, proposed Rule 3090 addresses three areas: (1) providing duplicate statements for brokerage accounts in which Association or Amex employees have a financial interest or can control trading; (2) loans by NASD members to Association or

Amex employees; and (3) gifts by NASD members to Association or Amex employees. Each of these areas is discussed in greater detail below.

(1) Employees' Brokerage Accounts

The NASD Code of Conduct imposes significant restrictions on employees' investments. Among other things, employees may not own stock of broker/dealers or companies that derive more than 25% of their gross revenues from broker/dealer activities, or stock purchased as part of an initial public offering. The NASD reviews duplicate statements for employees' brokerage accounts to ensure that employees have abided by these restrictions. Subsection (a) of proposed Rule 3090 is intended to help ensure that an NASD member receives and implements an instruction to send duplicate account statements to the NASD whenever the member has actual notice that an Association or Amex employee has a financial interest in, or controls trading in, an account. Currently, NASD employees are required to request the broker/dealers with which they maintain accounts to send duplicate account statements to the NASD. However, NASD rules currently do not impose a corresponding obligation on NASD members to obtain and implement such an instruction.

In administering the NASD Code of Conduct, the NASD routinely runs exception reports to determine whether duplicate statements are being received for all reported employee accounts. Employees for whom the NASD has not received duplicate account statements are reported to their department heads for follow-up. Each time exception reports are run, numerous employee accounts are listed as delinquent. In following up on such accounts, the NASD has frequently encountered instances in which NASD employees have repeatedly instructed their broker/dealer in

writing that duplicate statements are to be sent to the NASD, but the broker/dealer has failed to implement the instruction. In addition, there have been instances in which broker/dealers have refused to implement the instruction on the ground that they are not required to do so.

When employees' duplicate statement instructions are not implemented, the NASD has no means of monitoring trading in employee accounts. Currently, there is no rule that specifically requires member firms to implement such instructions.

Subsection (a) will remedy this deficiency by imposing on member firms an affirmative obligation to promptly obtain and implement a duplicate statement instruction when they have actual notice that an Association or Amex employee has a financial interest in, or controls trading in, an account. The information necessary to give members such actual notice is already included on the new account forms used by most broker/dealers, and on a standardized duplicate instruction form that Association and Amex employees can provide to their broker/dealers.

Proposed Subsection (a) imposes requirements that are analogous to those that other self-regulatory organizations already impose (*e.g.*, New York Stock Exchange Rule 407). In addition, the proposed requirements are similar to those currently imposed by NASD Conduct Rule 3050, which applies when an NASD member firm carries an account for a person associated with another broker/dealer.

It is contemplated that Subsection (a) would work as follows with respect to new accounts: when a new account form indicates that an NASD employee has an interest in a proposed new account, the NASD member firm would instruct the employee to obtain a duplicate instruction form (available on the NASD's corporate Intranet), complete the form, and provide it to the member

before the account is opened. The NASD expects that most employees will anticipate this request, and provide the member with the instruction at the time they seek to open the account. It will not be necessary for NASD officials to issue a letter authorizing the opening of each account.

With respect to existing accounts, Subsection (a) contemplates that Association and Amex employees will use the above-referenced duplicate instruction form to give NASD members actual notice of their interest in an existing account. A member receiving such a form would be expected to promptly implement the duplicate statement instruction.

The proposed rule change would apply prospectively to new accounts, and to those existing accounts as to which an NASD member has actual notice that an Association or Amex employee has financial interest or controls trading. NASD members will not be required to review existing accounts to identify those in which Association or Amex employees may have an interest or control trading.

(2) Loans to Employees

Subsection (b) of proposed Rule 3090 responds to an SEC staff recommendation that the NASD adopt a rule prohibiting NASD members from making loans to Association or Amex employees outside routine brokerage or banking relationships. The NASD Code of Conduct already prohibits employees from accepting loans from NASD members, Nasdaq issuers, or any person with whom the NASD transacts business. The proposed rule change will simply prevent NASD members from making loans to employees. Consistent with existing Code of Conduct provisions, the prohibition on loans would not apply to loans that are clearly motivated by a family

or personal relationship. Thus, for example, a registered representative would not be precluded from making a personal loan to an adult child who works at the NASD or Amex.

(3) Gifts to Employees

Subsection (c) of proposed Rule 3090 also responds to an SEC staff recommendation. The proposed rule change will parallel Code of Conduct provisions that permit employees to accept business gifts with an aggregate annual value of \$100 when no conflict of interest exists, but prohibit employees from accepting a business gift or courtesy from persons involved in regulatory matters in which the employee is involved. Specifically, the proposed rule change will state that, notwithstanding Conduct Rule 3060(a) (which generally permits NASD members to give business gifts with an aggregate annual value of \$100 to employees of others), members may not give business gifts or courtesies of more than nominal value to an Association or Amex employee who has responsibility for a specific regulatory matter that involves the member. For purposes of Subsection (c), "regulatory matter" would encompass such matters as examinations, disciplinary proceedings, membership applications, listing applications, delisting proceedings, and dispute-resolution proceedings involving a member. The proposed rule would permit members to give items of nominal value to employees responsible for regulatory matters affecting the member. Thus, for example, a member would be permitted to offer minor refreshments, such as a soft drink or coffee, to NASD Regulation employees conducting an on-site examination.

(b) Statutory Basis

NASD Regulation 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 Association'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. Specifically, the NASD believes that, by assisting the NASD in ensuring employee compliance with NASD ethical standards, the proposed rule change serves the public interest.

4. Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation 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

NASD Regulation does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

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

Not applicable.

8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission

Not applicable.

9. Exhibit

Completed notice of proposed rule change for publication in the Federal Register.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD Regulation has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD REGULATION, INC.

BY: _____
Joan C. Conley, Senior Vice President and
Corporate Secretary

Date: September 22, 2000

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-NASD-00-58)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Transactions Involving Association and American Stock Exchange Employees

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 , the National Association of Securities Dealers, Inc. (“NASD”), through its wholly owned subsidiary, NASD Regulation, Inc. (“NASD Regulation”) 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 Regulation. 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 Regulation is proposing to adopt Rule 3090 of the National Association of Securities Dealers, Inc. (“NASD”) to: (1) require NASD members to promptly obtain and implement a duplicate statement instruction whenever they have actual knowledge that an Association or American Stock Exchange (“Amex”) employee has a financial interest in, or controls trading in, an account; (2) prohibit NASD members from making loans to Association or Amex employees except in the context of a routine banking or brokerage relationship, or when it is clear

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

that a personal or family relationship motivates the loan; and (3) prohibit NASD members from giving business gifts or courtesies of more than nominal value to an Association or Amex employee who has responsibility for a specific regulatory matter (*e.g.*, examination, disciplinary proceeding, membership application, listing application, delisting proceeding, dispute-resolution proceeding) that involves the member. Below is the text of the proposed rule change. Proposed new language is in italics.

3090. Transactions Involving Association and American Stock Exchange Employees

(a) When a member has actual notice that an Association or American Stock Exchange employee has a financial interest in, or controls trading in, an account, the member shall promptly obtain and implement an instruction from the employee directing that duplicate account statements be provided by the member to the Association.

(b) No member shall directly or indirectly make any loan of money or securities to any Association or American Stock Exchange employee. Provided, however, that this prohibition does not apply to loans made in the context of disclosed, routine banking and brokerage agreements, or loans that are clearly motivated by a personal or family relationship.

(c) Notwithstanding the annual dollar limitation set forth in Conduct Rule 3060(a), no member shall directly or indirectly give, or permit to be given, anything of more than nominal value to any Association or American Stock Exchange employee who has responsibility for a regulatory matter that involves the member. For purposes of this subsection, the term "regulatory matter" includes, but is not limited to, examinations, disciplinary proceedings, membership applications,

listing applications, delisting proceedings, and dispute-resolution proceedings that involve the member.

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 Regulation 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 Regulation 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 NASD Code of Conduct imposes detailed ethics and conflict-of-interest requirements on Association employees (*i.e.*, employees of NASD, Inc. and all of its subsidiary and affiliated companies). The NASD is proposing a new rule, NASD Conduct Rule 3090, that will impose parallel requirements on NASD members in their dealings with Association and American Stock Exchange ("Amex") employees. The Amex, whose employees will become subject to the NASD Code of Conduct in October 2000, has filed rule a proposal (No. SR-Amex-00-23) that will make parallel changes to Amex rules.

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The proposed rule would apply prospectively to new accounts, and to those existing accounts as to which an NASD member has actual notice that an Association or Amex employee has financial interest or controls trading. NASD members will not be required to review existing accounts to identify those in which Association or Amex employees may have an interest or control trading.

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(b) Statutory Basis

NASD Regulation 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 Association'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. Specifically, the NASD believes that, by assisting the NASD in ensuring employee compliance with NASD ethical standards, the proposed rule change serves the public interest.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD Regulation 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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- A. by order approve such proposed rule change, or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

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 the 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