

### INFORMATIONAL

# Restrictions On Unregistered Persons

## Withdrawal Of Proposed Rule And Reminder Of Restrictions On Use Of Unregistered Persons

### 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.

- Internal Audit
- Legal & Compliance
- Operations
- Registered Representatives
- Registration
- Senior Management
- Training

### KEY TOPICS

- Cold Calling
- Telemarketing
- Unregistered Persons

### Executive Summary

In light of recent federal law, NASD Regulation, Inc. (NASD Regulation<sup>SM</sup>) has withdrawn its rule proposal addressing the permissible marketing activities and supervision of unregistered persons. NASD Regulation does not anticipate rule making in this area at the present time. With this *Notice*, NASD Regulation is reminding members of its current policy with respect to the permissible marketing activities of unregistered persons, as previously set forth in *Notice to Members 88-50 (NtM 88-50)*.

### Questions/Further Information

Questions concerning this *Notice* may be directed to Gary L. Goldsholle, Associate General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8104.

### Background And Summary

*NtM 88-50* provides guidance on the circumstances under which an unregistered person may contact a prospective brokerage customer. Specifically, *NtM 88-50* states that unregistered persons may contact prospective customers for three purposes only:

- (1) to extend invitations to firm-sponsored events;
- (2) to inquire whether the customer wishes to discuss investments with a registered person; and
- (3) to inquire whether the customer wishes to receive investment literature.

*NtM 88-50* also contains supervisory guidelines, including requirements for orientation and

training, background investigations, and a limitation on compensation of unregistered personnel.

In an effort to replace *NtM 88-50*, in September 1997, NASD Regulation issued *Notice to Members 97-58* requesting comment on a proposed Interpretive Material regarding the registration of certain persons who solicit securities business on behalf of member firms. In short, the proposal would have required all persons associated with a member who communicate with the public for the purpose of soliciting the purchase of securities or related services or identifying prospective customers to register as a representative of the member firm.

In 1998, based upon the comments received and input provided by NASD Regulation standing committees, NASD Regulation developed an alternative proposal that codified the restrictions governing the permissible activities of unregistered persons contained in *NtM 88-50* and established comprehensive supervisory responsibilities of members towards such persons. The proposal was filed with the Securities and Exchange Commission on July 2, 1998, and published for comment in the *Federal Register* on December 18, 1998.<sup>1</sup>

The proposal encountered opposition from banks and bank-affiliated member firms, which asserted, among other things, that the National Association of Securities Dealers, Inc. (NASD<sup>®</sup>) did not have jurisdiction over bank employees. NASD Regulation disagreed and believed that the restrictions on a member's use of unregistered persons should apply uniformly without regard to whether such persons are also employees of a bank.

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This issue was resolved with the passage of the Gramm-Leach-Bliley Financial Services Modernization Act (GLB), which was signed into law on November 12, 1999. The GLB contains provisions that, effective May 13, 2001, repeal the general bank exclusion from the definition of broker under the Securities Exchange Act of 1934. In its place, the GLB leaves a number of targeted exclusions, including one for “networking” or “third party brokerage” arrangements. A networking or third party brokerage arrangement is one in which a bank enters into a contract or other written arrangement with a registered broker/dealer for the provision of brokerage services.

Under the GLB, a bank that enters into a third party brokerage arrangement will be exempt from registration as a broker only if it meets certain conditions. These conditions include that bank employees (other than persons associated with a member who are qualified pursuant to the rules of a self-regulatory organization) perform only clerical or ministerial functions in connection with brokerage transactions including scheduling appointments with associated persons, except that the employees may forward customer funds or securities, and may describe in general terms the types of investment vehicles available from the bank and the broker/dealer. The Conference Report to the GLB in discussing the networking exclusion states that NASD Regulation’s proposal concerning the permissible activities of unregistered persons is inconsistent with the new legislation and should be revised to exempt banks and their employees from the proposal’s coverage.<sup>2</sup>

In view of the language of the GLB and the Conference Report, NASD Regulation has withdrawn the proposal. Rather than continue to pursue adoption of a rule at this time, NASD Regulation has decided to remind members of the restrictions on the use of unregistered persons as set forth in *NtM 88-50*.

### Permissible Activities Of Unregistered Persons

NASD Rule 1031(b) defines a “representative” as “[p]ersons associated with a member . . . who are engaged in the investment banking or securities business for the member including the functions of supervision, solicitation or conduct of business in securities . . .” This definition has been consistently interpreted by the NASD to require registration of persons who engage in activities that only constitute a portion of registered representatives’ traditional dealings with public customers, including persons who solicit accounts on behalf of members.

As stated in *NtM 88-50*, and reiterated here, unregistered persons may contact prospective customers for three purposes only:

- extending invitations to firm-sponsored events at which any substantive presentations and account or order solicitation will be conducted by appropriately registered personnel;
- inquiring whether the prospective customer wishes to discuss investments with a registered person; and
- determining whether the prospective customer wishes to receive investment literature from the firm.

In addition, the following guidelines are applicable to firms employing unregistered persons to perform these functions:

- (1) Pursuant to Rule 1031, unregistered persons may not discuss general or specific investment products or services offered by the firm, pre-qualify prospective customers as to financial status and investment history and objectives, or solicit new accounts or orders.
- (2) The member should provide unregistered persons with orientation and training that specifically addresses the limitations of such persons’ activities, the regulatory consequences of exceeding these limitations, and the fact that such persons are associated persons of the member, subject to the rules of the NASD and its disciplinary authority.
- (3) The member should conduct a reasonable investigation of such persons’ backgrounds to determine that they are not statutorily disqualified from becoming associated with the member.
- (4) Unregistered persons are regarded as employees of the member and should not be compensated on any basis other than a salary or hourly wage.
- (5) The member should take reasonable steps to ensure that the activities of unregistered persons are consistent with applicable state statutes and rules and with the rules of other self-regulatory organizations.
- (6) The member should be able, upon request, to demonstrate

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that its supervisory procedures include procedures reasonably designed to prevent violative conduct by unregistered persons.

### Clarification Of Guidelines

In addition, NASD Regulation is making several clarifications with respect to these guidelines, which were originally published in *NtM 88-50*. With respect to item (1), above, unregistered persons may describe in general terms the types of investment vehicles available from the member, but may not discuss the attributes or merits of

any particular investment vehicle or service or class of vehicles or services. With respect to item (4), above, the payment of performance bonuses or other forms of incentive compensation, such as through participation in a member's profit sharing plan, are permitted so long as such bonuses or incentives are not tied to transactions, commission activity, or referrals generated by the unregistered person.

Members are advised to review the activities of unregistered persons to ascertain that such persons are not functioning in a manner requiring registration.

### Endnotes

<sup>1</sup>63 Fed. Reg. 70173 (Dec. 18, 1998).

<sup>2</sup>See H.R. Conf. Rep. No. 434, 106th Cong., 1st Sess., 145 Cong. Rec. H11,255 (1999).

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### INFORMATIONAL

## Margin Requirements

SEC Approves Proposed Rule Change Relating To Margin For Exempted Borrowers, Good Faith Accounts, Joint Back Office Arrangements, Control And Restricted Securities, And Options Transactions; **Effective Date: August 21, 2000**

### SUGGESTED ROUTING

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- Executive Representatives
- Institutional
- Legal & Compliance
- Operations
- Options
- Systems

### KEY TOPICS

- Margin
- NASD Rule 2520
- Options

### Executive Summary

On May 30, 2000, the Securities and Exchange Commission (SEC) approved amendments to National Association of Securities Dealers, Inc. (NASD<sup>®</sup>) Rule 2520 relating to margin requirements for exempted borrowers, good faith accounts, joint back office (JBO) arrangements, control and restricted securities, and options transactions.<sup>1</sup> The amendments become effective on August 21, 2000. There is a six-month phase-in period for the implementation of the amendments relating to JBO arrangements.

Questions concerning this *Notice* may be directed to Susan DeMando, Director, Financial Operations, Member Regulation, NASD Regulation, Inc. (NASD Regulation<sup>SM</sup>) at (202) 728-8411; or Stephanie M. Dumont, Assistant General Counsel, Office of General Counsel, NASD Regulation, at (202) 728-8176.

Attachment A includes the text of the amendments to Rule 2520.

### Highlights Of Rule Changes

The significant changes to Rule 2520 are discussed below.

#### **Exempted Borrowers And Good Faith Accounts**

Under recent changes to Regulation T, the Federal Reserve Board has created a new account category called the "good faith account" to replace the "non-purpose," "arbitrage," and "government securities" accounts.<sup>2</sup> In the good faith account, a customer may purchase certain securities (exempted securities, non-equity securities, money market mutual funds, and exempted securities mutual funds)

on "good faith" margin (the amount of margin specified by the creditor in the exercise of sound credit judgment) or the margin specified by the applicable regulatory authority, whichever is greater. Regulation T no longer specifies initial margin, payment, and liquidation time frames for transactions in these securities in a good faith account.

NASD Regulation believes that transactions in good faith accounts can raise the same financial concerns as transactions in cash and margin accounts. Accordingly, the amendments to Rule 2520(c) require all accounts, including good faith accounts, to maintain margin as required by NASD Rule 2520. Cash accounts will continue to be subject only to certain specific requirements applicable to cash accounts, not to the overall requirements of the rule.

In addition, the Federal Reserve Board established a classification of exempted borrowers that are exempt from Regulation T. An "exempted borrower," as defined in Regulation T, is a broker/dealer of which "a substantial portion of whose business consists of transactions with persons other than brokers or dealers."<sup>3</sup> The amendments codify this exemption from Regulation T by excluding "exempted borrowers," as defined in Regulation T, from the definition of "customer" in NASD Rule 2520(a)(3), except for the proprietary account of a broker/dealer carried by a member pursuant to NASD Rule 2520(e)(6). Thus, proprietary accounts of an introducing member that are carried or cleared by another member will remain subject to the equity requirements of NASD Rule 2520(e)(6).

### **Joint Back Office Arrangements**

Section 220.7(c) of Regulation T allows special margin treatment for broker/dealers without clearing operations, known as “JBO participants,” that invest in a “clearing and servicing” broker/dealer, known as a “JBO broker.” The amendments provide certain regulatory requirements for initiating and maintaining JBO arrangements established pursuant to Section 220.7 of Regulation T, as follows. These amendments should be phased in over the next six months and must be implemented by February 26, 2001.

A JBO broker must be a clearing or carrying firm in accordance with the requirements of Regulation T. Under the amendments, a JBO broker is required to:

- Notify the NASD in writing<sup>4</sup> prior to establishing a JBO arrangement.
- Maintain a minimum tentative net capital<sup>5</sup> of \$25 million, unless the JBO broker's primary business consists of the clearance of options market-maker accounts,<sup>6</sup> then it may elect to maintain a minimum net capital<sup>7</sup> of \$7 million, provided it also includes gross deductions for JBO participant accounts in its ratio of gross options market-maker deductions to net capital pursuant to SEC Rule 15c3-1 (Net Capital Rule).
- Notify the NASD promptly in writing<sup>8</sup> if tentative net capital or net capital falls below the requirements outlined above and take action to correct such deficiency within three business days or, if it fails to do so, the JBO broker is prohibited from accepting new transactions pursuant to the JBO arrangement.

- Deduct from its net capital, haircut requirements pursuant to the Net Capital Rule that are in excess of the equity maintained in the accounts of the JBO participants.

- Maintain a written risk analysis methodology for assessing the amount of credit extended to JBO participants. Minimum guidelines for acceptable risk procedures should include the following:

- ◆ Procedures for obtaining and reviewing appropriate account documentation and financial information;
- ◆ Procedures and guidelines for the determination, review, and approval of credit limits;
- ◆ Procedures and guidelines for monitoring credit risk exposure to the organization relating to JBO participants;
- ◆ Procedures and guidelines for the use of stress testing of accounts in order to monitor market risk exposure; and
- ◆ Procedures providing for the regular review and testing of these risk management procedures by an independent unit such as internal audit, risk management, or other comparable group.

A JBO participant must be a registered broker/dealer subject to the Net Capital Rule. The JBO participant is required to:

- Maintain an ownership interest in the JBO broker pursuant to Regulation T of the Federal Reserve Board; and
- Maintain a minimum net liquidating equity of \$1 million in the JBO account, exclusive of the

JBO participant's ownership interest in the JBO broker.

If the JBO participant's liquidating equity falls below \$1 million, the equity deficiency must be met within five business days in order to ensure continued eligibility as a JBO participant. A JBO participant that loses its JBO participant status generally would become subject to customer margin account requirements pursuant to Regulation T, if applicable, and margin requirements pursuant to other provisions of Rule 2520.

### **Control And Restricted Securities**

Rule 2520(e)(8)(C)(ii) has been modified to address an anomaly currently within the “Concentration Reduction” provision, which imposes a higher requirement on accounts that have deposited more control and restricted securities than are required to collateralize the extension of credit. To eliminate this unintended penalty, the amount of “excess securities,” as defined in the amended Rule 2520, will be excluded from the Concentration Reduction calculation.<sup>9</sup> Thus, the Concentration Reduction calculation will be performed on an aggregate position that is only as large as the collateral necessary to support a margin loan of 50 percent.

In addition, the amendments expand the exception in paragraph (e)(8) to include all restricted securities that are then saleable, including affiliate securities, pursuant to Rules 144(k), 145(d)(2), or 145(d)(3) of the Securities Act of 1933. Accordingly, those customer-owned, restricted securities that are then saleable and can be sold under SEC Rule 144(k) would be subject to the same maintenance margin requirements that currently apply to ordinary stock (25 percent).

### **Broker/Dealer Margin Requirements**

Subparagraphs (e)(5) and (e)(6) of Rule 2520 currently require a carrying broker/dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker, or broker/dealer and the required maintenance margin under NASD Rule 2520. The amendments to subparagraphs (e)(5) and (e)(6) require the carrying broker/dealer to deduct from its net capital the difference between the equity maintained in the account of a specialist, market maker, or broker/dealer and the required haircut in accordance with the Net Capital Rule. For example, in the case of a long position in an equity security, the amendments require a carrying broker to compute its net capital deduction for deficient specialist, market maker, and broker/dealer accounts based on the 15 percent haircut requirement of paragraph (c)(2)(vi)(J) of the Net Capital Rule, rather than the 25 percent maintenance margin requirement of NASD Rule 2520(c)(1).

### **Options Transactions**

Rule 2520(f)(2)(L) incorporates provisions currently contained in Regulation T regarding "exclusive designation." This provision will allow a customer to designate which security position in an account to use to cover the requested margin at the time the option order is entered, provided the member offers such a service. NASD Rule 2520(f)(2)(M)(i) permits options transactions in customer cash accounts if the transaction is permissible under Section 220.8 of Regulation T.

### **Effective Date Of Amendments**

These amendments become effective on August 21, 2000. However, there is a six-month phase-in period for the amendments relating to JBO arrangements, which must be implemented by February 26, 2001.

### **Endnotes**

<sup>1</sup> See Securities Exchange Act Release No. 42858 (May 30, 2000), 65 Fed. Reg. 36194 (June 7, 2000) (File No. SR-NASD-99-05).

<sup>2</sup> See Board of Governors of the Federal Reserve System Docket Nos. R-0905, R-0923, and R-0944, 63 Fed. Reg. 2806 (January 16, 1998).

<sup>3</sup> 12 CFR 220.2.

<sup>4</sup> Notification should be made to the appropriate NASD District Office and to the Financial Operations Department, NASD Regulation, 1735 K Street, NW, Washington, DC 20006.

<sup>5</sup> The term "tentative net capital" generally refers to net capital before haircuts and undue concentration charges on proprietary securities and options positions. Haircuts are specified percentages of the market value of a broker/dealer's proprietary securities by which a broker/dealer must reduce its net worth under Rule 15c3-1 under the Securities Exchange Act of 1934 (the "Net Capital Rule" or "SEC Rule 15c3-1").

<sup>6</sup> The clearance of options market-maker accounts will be deemed a broker/dealer's primary business if a minimum of 60 percent of the aggregate deductions in the broker/dealer's ratio of gross options market-maker deductions to net capital (including gross deductions for JBO participant accounts) are options market-maker

deductions. Subparagraph (c)(2)(x) of the Net Capital Rule limits the amount of specialist and market-maker options positions a firm may guarantee, endorse, or carry to a ratio of 10 to 1 of options market maker and specialist deductions to net capital. In addition, subparagraph (a)(6) of the Net Capital Rule exempts an option market maker and specialist from the haircut provisions of the Net Capital Rule provided that, among other things, the firm maintains liquidating equity in its account equal to the percentage described in subparagraph (a)(6)(iii)(A) of the Net Capital Rule.

<sup>7</sup> The term "net capital" is defined under the Net Capital Rule and is generally calculated by deducting illiquid assets from a firm's "net worth," as determined under Generally Accepted Accounting Principles (GAAP), adding to that amount properly subordinated debt under Appendix D of the Net Capital Rule, and further deducting haircuts from securities held in the firm's proprietary accounts.

<sup>8</sup> Notification should be made to the appropriate NASD District Office and to the Financial Operations Department, NASD Regulation, 1735 K Street, NW, Washington, DC 20006.

<sup>9</sup> The term "excess securities" is defined as the amount of securities, if any, by which the aggregate position in control and restricted securities of any one issue exceeds the aggregate amount of securities that would be required to support the aggregate credit extended on such control and restricted securities if the applicable margin requirement were 50 percent.

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## ATTACHMENT A

### Text Of Amendments

(Note: New language is underlined; deletions are in brackets.)

#### 2520. Margin Requirements

##### (a) Definitions

For purposes of this paragraph, the following terms shall have the meanings specified below:

(1) – (2) No Change

(3) The term “customer” means any person for whom securities are purchased or sold or to whom securities are purchased or sold whether on a regular way, when issued, delayed or future delivery basis. It will also include any person for whom securities are held or carried and to or for whom a member extends, arranges or maintains any credit. The term will not include the following: (A) a broker or dealer from whom a security has been purchased or to whom a security has been sold for the account of the member or its customers[.], or (B) an “exempted borrower” as defined by Regulation T of the Board of Governors of the Federal Reserve System (“Regulation T”), except for the proprietary account of a broker/dealer carried by a member pursuant to paragraph (e)(6) of this Rule.

(4) – (8) No Change

##### (b) Initial Margin

For the purpose of effecting new securities transactions and commitments, the customer shall be required to deposit margin in cash and/or securities in the

account which shall be at least the greater of:

(1) the amount specified in Regulation T [of the Board of Governors of the Federal Reserve System]; or

(2) the amount specified in paragraph (c)(3) of this Rule; or

(3) such greater amount as the Association may from time to time require for specific securities; or

(4) equity of at least \$2,000 except that cash need not be deposited in excess of the cost of any security purchased (this equity and cost of purchase provision shall not apply to “when distributed” securities in a cash account).

Withdrawals of cash or securities may be made from any account which has a debit balance, “short” position or commitments, provided it is in compliance with Regulation T [of the Board of Governors of the Federal Reserve System] and after such withdrawal the equity in the account is at least the greater of \$2,000 or an amount sufficient to meet the maintenance margin requirements of this paragraph.

##### (c) Maintenance Margin

The margin which must be maintained in all [margin] accounts of customers, except for cash accounts subject to other provisions of this rule, shall be as follows:

(1) 25 percent of the current market value of all securities “long” in the account; plus

(2) \$2.50 per share or 100 percent of the current market value, whichever amount is greater, of each stock “short” in

the account selling at less than \$5.00 per share; plus

(3) \$5.00 per share or 30 percent of the current market value, whichever amount is greater, of each stock “short” in the account selling at \$5.00 per share or above; plus

(4) 5 percent of the principal amount or 30 percent of the current market value, whichever amount is greater, of each bond “short” in the account; plus

(5) In the case of securities listed on the Emerging Company Marketplace of the American Stock Exchange (AMEX), 100 percent of the market value in cash, of each security held “long” in the account, unless the AMEX determines that the security satisfies the criteria enumerated in Sections 220.17(a) and (b) of Regulation T of the Board of Governors of the Federal Reserve System for inclusion and continued inclusion on the List of OTC Margin Stocks, except for the requirement relating to the number of dealers in Sections 220.17(a)(1) and (b)(1)].

(d) No Change

(e) Exceptions to Rule

The foregoing requirements of this [paragraph] Rule are subject to the following exceptions:

(1) No Change

(2) Exempted Securities, Marginable Corporate Debt Securities and Baskets

(A) – (B) No Change

(C) Non-Convertible Corporate Debt Securities

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On any positions in non-convertible corporate debt securities, which are listed or traded on a registered national securities exchange or qualify as an "OTC margin bond," as defined in Section 220.2(t) of Regulation T [of the Board of Governors of the Federal Reserve System], the margin to be maintained shall be 20 percent of the current market value or 7 percent of the principal amount, whichever amount is greater, except on mortgage related securities as defined in Section 3(a)(41) of the Act the margin to be maintained for an exempt account shall be 5 percent of the current market value. For purposes of this subparagraph, an exempt account shall be defined as a member, non-member broker/dealer, "designated account" or any person having net tangible assets of at least sixteen million dollars.

(D) – (F) No Change

(3) Joint Accounts in Which the Carrying Member or a Partner or Stockholder Therein Has an Interest

In the case of a joint account carried by a member in which such member, or any partner, or stockholder (other than a holder of freely transferable stock only) of such member participates with others, each participant other than the carrying member shall maintain an equity with respect to such interest pursuant to the margin provisions of this paragraph as if such interest were in a separate account.

Pursuant to the Rule 9600 Series, the Association may grant an exemption from the

provisions of paragraph (e)(3), if the account is[.]

[(A)] confined exclusively to transactions and positions in exempted securities[.]

(B) maintained as a Market Functions Account conforming to the conditions of Section 220.12(e) (Odd-lot dealers) of Regulation T of the Board of Governors of the Federal Reserve System; or

(C) maintained as a Market Functions Account conforming to the conditions of Section 220.12(c) (Underwritings and Distributions) of Regulation T of the Board of Governors of the Federal Reserve System and each other participant margins his share of such account on such basis as the Association may prescribe[.]

(4) No Change

(5) Specialists' and Market Makers' Accounts

(A) A member may carry the account of an "approved specialist or market maker," which account is limited to specialist or market making transactions, upon a margin basis which is satisfactory to both parties. The amount of any deficiency between the equity in the account and the [margin required by the other provisions of this paragraph and the] haircut requirements pursuant to SEC Rule 15c3-1 shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

For the purpose of this subparagraph, the term "approved specialist or market maker" means either:

(i) a specialist or market maker, who is deemed a specialist for all purposes under the Act and who is registered pursuant to the rules of a national securities exchange; or

(ii) an OTC market maker or third market maker, who meets the requirements of Section 220.7(g)(5)[12(d)] of Regulation T [of the Board of Governors of the Federal Reserve System].

(B) In the case of a joint account carried by a member in accordance with subparagraph (i) above in which the member participates, the equity maintained in the account by the other participants may be in any amount which is mutually satisfactory. The amount of any deficiency between the equity maintained in the account by the other participants and their proportionate share of the [margin required by the other provisions of this paragraph] the haircut requirements pursuant to SEC Rule 15c3-1 shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

(6) Broker/Dealer Accounts

(A) A member may carry the proprietary account of another broker/dealer, which is registered with the Commission, upon a margin basis which is satisfactory to both parties, provided the requirements of Regulation T [of the Board of Governors of the Federal Reserve System] are adhered to and the account is not carried in a deficit equity condition. The amount of any deficiency between the equity

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maintained in the account and the [margin required by the other provisions of this paragraph] haircut requirements pursuant to SEC Rule 15c3-1 shall be charged against the member's net capital when computing net capital under SEC Rule 15c3-1.

### (B) Joint Back Office Arrangements

An arrangement may be established between two or more registered broker/dealers pursuant to Regulation T Section 220.7, to form a joint back office ("JBO") arrangement for carrying and clearing or carrying accounts of participating broker/dealers. Members must provide written notification to the Association prior to establishing a JBO arrangement.

(i) A carrying and clearing, or carrying member must:

a. maintain a minimum tentative net capital of \$25 million as computed pursuant to SEC Rule 15c3-1, except that a member whose primary business consists of the clearance of options market-maker accounts may carry JBO accounts provided that it maintains a minimum net capital of \$7 million as computed pursuant to SEC Rule 15c3-1. In addition, the member must include in its ratio of gross options market maker haircuts required by the provisions of SEC Rule 15c3-1 gross deductions for JBO participant accounts. Clearance of option market maker accounts shall be deemed a broker/dealer's primary business if a

minimum of 60% of the aggregate deductions in the above ratio are options market maker deductions. In the event that a carrying and clearing, or a carrying member's tentative net capital, or net capital, respectively, has fallen below the above requirements, the firm shall:  
1. promptly notify the Association in writing of such deficiency, 2. take appropriate action to resolve such deficiency within three consecutive business days, or not permit any new transactions to be entered into pursuant to the JBO arrangement;

b. maintain a written risk analysis methodology for assessing the amount of credit extended to participating broker/dealers which shall be made available to the Association on request; and

c. deduct from net capital haircut requirements pursuant to SEC Rule 15c3-1 amounts in excess of the equity maintained in the accounts of participating broker/dealers.

(ii) A participating broker/dealer must:

a. be a registered broker/dealer subject to the SEC's net capital requirements;

b. maintain an ownership interest in the carrying/clearing member organization pursuant to Regulation T of the Federal Reserve Board, Section 220.7; and

c. maintain a minimum liquidating equity of \$1 million in the JBO arrangement exclusive of the ownership interest established in (ii)b. above. When the minimum liquidating equity decreases below the \$1 million requirement, the participant must deposit an amount sufficient to eliminate this deficiency within 5 business days or be subject to margin account requirements prescribed for customers in Regulation T, and the margin requirements pursuant to the other provisions of this Rule.

### (7) Nonpurpose Credit

In a nonsecurities credit account, a member may extend and maintain nonpurpose credit to or for any customer without collateral or on any collateral whatever, provided,

(A) the account is recorded separately and confined to the transactions and relations specifically authorized by Regulation T [of the Board of Governors of the Federal Reserve System];

(B) the account is not used in any way for the purpose of evading or circumventing any regulation of the Association or of the Board of Governors of the Federal Reserve System; and

(C) the amount of any deficiency between the equity in the account and the margin required by the other provisions of this paragraph shall be charged against the member's net capital as provided in SEC Rule 15c3-1.

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The term "nonpurpose credit" means an extension of credit other than "purpose credit" as defined in Section 220.2[(u)] of Regulation T [of the Board of Governors of the Federal Reserve System].

### (8) Shelf-Registered, Control and Restricted Securities

#### (A) No Change

(B) Control and Restricted Securities—The equity in accounts of customers for control securities and other restricted securities of issuers who continue to maintain a consistent history of filing annual and periodic reports in timely fashion pursuant to the formal continuous disclosure system under the Act, which are subject to Rule 144 or 145(d) under the Securities Act of 1933, shall be 40 percent of the current market value of such securities "long" in the account, provided the member:

(i) in computing net capital, deducts any margin deficiencies in customers' accounts based upon a margin requirement as specified in subparagraph (C)(ii) [(iii)] below for such securities and values only that amount of such securities which are then salable under Rule 144 or 145(d) under the Securities Act of 1933 in conformity with all of the applicable terms and conditions thereof, for purposes of determining such deficiencies; and

#### (ii) No Change

(C) Additional Requirements on Shelf-Registered Securities and Control and Restricted

Securities - A member extending credit on shelf-registered, control and other restricted securities in margin accounts of customers shall be subject to the following additional requirements:

(i) The Association may at any time require reports from members showing relevant information as to the amount of credit extended on shelf-registered, control and restricted securities and the amount, if any, deducted from net capital due to such security positions.

(ii) Concentration Reduction. A concentration exists whenever the aggregate position in control and restricted securities of any one issue, excluding excess securities (as defined below), exceeds:

a. 10 percent of the outstanding shares or

b. 100 percent of the average weekly volume during the preceding three-month period. Where a concentration exists, for purposes of computing subparagraph (B)(i) above, the margin requirement on such securities shall be, based on the greater of (ii)a. or b. above, as specified below:

\*\*\*No Change to Table \*\*\*

For purposes of this subparagraph (e)(8)(C)(ii), "excess securities" shall mean the amount of securities, if any, by which the aggregate position in control and restricted securities of any one issue

exceeds the aggregate amount of securities that would be required to support the aggregate credit extended on such control and restricted securities if the applicable margin requirement were 50%.

(D) Restricted Securities - Securities either:

(i) [held by non-affiliates of the issuer which are] then salable [by the non-affiliate] pursuant to the terms and conditions of Rule 144(k) under the Securities Act of 1933, or

(ii) [which have been acquired by non-affiliates of the issuer in connection with a Rule 145(a) transaction under the Securities Act of 1933 which are] then salable [by such non-affiliate] pursuant to the terms and conditions of Rule 145(d)(2) or (d)(3) under such Act,

shall not be subject to the provisions of this subparagraph [(H)] (e)(8), provided that the issuer continues to maintain a consistent history of filing annual and periodic reports in timely fashion pursuant to the formal continuous disclosure system under the Act.

(f) Other Provisions

(1) – (2)(H)(iii) No Change

(2)(H)(iv) Where a put or call is carried "short" in the account of a customer against a letter of guarantee in form satisfactory to the Association and issued by a third party custodian bank or trust company (the guarantor), which letter of guarantee is held in the account at the time the put or call is written, or is received in the

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account promptly thereafter, no margin need be required on the put or call.

In the case of a call on a broad index stock group, the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter either cash, cash equivalents, one or more qualified securities, or any combination thereof, having an aggregate market value, computed as at the close of business on the day the call is written, of not less than 100 percent of the aggregate current index value computed as at the same time and that the guarantor will promptly pay the member the exercise settlement amount in the event the account is assigned an exercise notice. The letter of guarantee may provide for substitution of qualified securities held as collateral provided that the substitution shall not cause the value of the qualified securities held to be diminished. A qualified security means an equity security, other than a warrant, right or option, that is traded on any national securities exchange; or any equity security, other than a warrant, listed in the current list of Over-the-Counter Margin Stocks as published by the Board of Governors of the Federal Reserve System.

In the case of a call on any other option contract, the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter, the underlying security (or a security immediately convertible into the underlying security without the payment of money) or foreign currency and that the guarantor will promptly deliver to the member the underlying security or foreign

currency in the event the account is assigned an exercise notice.

In the case of a put on an option contract (including a put on a broad index stock group), the letter of guarantee must certify that the guarantor holds for the account of the customer as security for the letter, cash or cash equivalents which have an aggregate market value, computed as at the close of business on the day the put is written, of not less than 100 percent of the aggregate exercise price of the put and that the guarantor will promptly pay the member the exercise settlement amount (in the case of a put on a broad index stock group) or the aggregate exercise price (in the case of any other put on an option contract) in the event the account is assigned an exercise notice. Cash equivalents shall mean those instruments referred to in Section 220.2 of Regulation T [of the Board of Governors of the Federal Reserve System].

(f)(2)(I) – (K) No Change

(L) Exclusive designation - A customer may designate at the time an option order is entered which security position held in the account is to serve in lieu of the required margin, if such service is offered by the member; or the customer may have a standing agreement with the member as to the method to be used for determining on any given day which security position will be used in lieu of the margin to support an option transaction. Any security held in the account which serves in lieu of the required margin for a short put or short call shall be unavailable to support any

other option transaction in the account.

(M) Cash account transactions - A member may make option transactions in a customer's cash account, provided that the transaction is permissible under Regulation T, Section 220.8.

(3) "When Issued" and "When Distributed" Securities

(A) Margin Accounts

The margin to be maintained on any transaction or net position in each "when issued" security shall be the same as if such security were issued.

Each position in a "when issued" security shall be margined separately and any unrealized profit shall be of value only in providing the amount of margin required on that particular position.

When an account has a "short" position in a "when issued" security and there are held in the account securities upon which the "when issued" security may be issued, such "short" position shall be marked to the market and the balance in the account shall for the purpose of this [paragraph (c)] Rule be adjusted for any unrealized loss in such "short" position.

(B) Cash Accounts

On any transaction or net position resulting from contracts for a "when issued" security in an account other than that of a member, non-member broker/dealer, or a "designated account," equity must be maintained equal to the margin required were such transaction

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or position in a margin account.

On any net position resulting from contracts for a "when issued" security made for or with a non-member broker/dealer, no margin need be required, but such net position must be marked to the market.

On any net position resulting from contracts for a "when issued" security made for a member or for or with a "designated account," no margin need be required and such net position need not be marked to the market. However, where such net position is not marked to the market, an amount equal to the loss at the market in such position shall be charged against the member's net capital as provided in SEC Rule 15c3-1.

The provisions of this subparagraph [(B)](f)(3) shall not apply to any position resulting from contracts on a "when issued" basis in a security:

(i) which is the subject of a primary distribution in connection with a bona fide offering by the issuer to the general public for "cash," or

(ii) which is exempt by the Association as involving a primary distribution.

The term "when issued" as used herein also means "when distributed."

(f)(4) – (5) No Change

(f)(6) Time Within Which Margin or "Mark to Market" Must Be Obtained

The amount of margin or "mark to market" required by any provision of this [paragraph (c)] Rule shall be obtained as promptly as possible and in any event within fifteen business days from the date such deficiency occurred, unless the Association has specifically granted the member additional time.

(f)(7) Practice of Meeting Regulation T Margin Calls by Liquidation Prohibited

When a "margin call," as defined in Section 220.2[(1)] of Regulation T [of the Board of Governors of the Federal Reserve System], is required in a customer's account, no member shall permit a customer to make a practice of either deferring the deposit of cash or securities beyond the time when such transactions would ordinarily be settled or cleared, or meeting the margin required by the liquidation of the same or other commitments in the account.

This prohibition on liquidations shall only apply to those accounts that, at the time of liquidation, are not in compliance with the equity to be maintained pursuant to the provisions of this Rule.

(f)(8)(A) No Change

(f)(8)(B) Day-Trading

The term "day-trading" means the purchasing and selling of the same security on the same day. A "day-trader" is any customer whose trading shows a pattern of day-trading.

Whenever day-trading occurs in a customer's margin account the margin to be maintained

shall be the margin on the "long" or "short" transaction, whichever occurred first, as required pursuant to the other provisions of this Rule. When day-trading occurs in the account of a "day-trader" the margin to be maintained shall be the margin on the "long" or "short" transaction, whichever occurred first, as required by Regulation T [of the Board of Governors of the Federal Reserve System] or as required pursuant to the other provisions of this Rule, whichever amount is greater.

When the equity in a customer's account, after giving consideration to the other provisions of this Rule, is not sufficient to meet the requirements of subparagraph (i) or (ii) hereof, additional cash or securities must be received into the account to meet any deficiency within seven business days of the trade date.

(9) Free-Riding in Cash Accounts Prohibited

No member shall permit a customer (other than a broker/dealer or a "designated account") to make a practice, directly or indirectly, of effecting transactions in a cash account where the cost of securities purchased is met by the sale of the same securities. No member shall permit a customer to make a practice of selling securities with them in a cash account which are to be received against payment from another broker/dealer where such securities were purchased and are not yet paid for. A member transferring an account which is subject to a Regulation T 90-day freeze to another member firm

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shall inform the receiving member of such 90-day freeze.

The provisions of Section 220.8(c) of Regulation T [of the Board of Governors of the Federal Reserve System] dictate

the prohibitions and exceptions against customers' free-riding. Members may apply to the Association in writing for waiver of a 90-day freeze not exempted by Regulation T.

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## INFORMATIONAL

### Decimalization

#### NASD And Exchanges Submit Decimalization Plan To The SEC

## 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.

- Legal & Compliance
- Operations
- Options
- Registered Representatives
- Senior Management
- Technology
- Trading & Market Making

## KEY TOPICS

- Decimalization

### Executive Summary

The National Association of Securities Dealers, Inc. (NASD®) and the exchanges recently submitted a decimalization plan to the Securities and Exchange Commission (SEC). The plan has not yet been approved by the SEC.

Members are reminded to prepare their own written decimalization plans that address their conversion to decimal pricing.

### Questions/Further Information

Questions regarding this Notice should be directed to the Decimalization Program Management Office at (888) 227-1330 or via e-mail at [decimals@nasd.com](mailto:decimals@nasd.com).

For the most recent decimalization news and developments, visit the NASD Web Site ([www.nasd.com](http://www.nasd.com)) and click on the decimalization link. Additional decimalization information is available on the Securities Industry Association's (SIA) Web Site, located at [www.sia.com](http://www.sia.com).

### NASD & Exchanges' Decimalization Plan

On July 24, 2000, the NASD and the exchanges submitted their decimalization plan to the SEC as requested in an order issued by the SEC on June 8, 2000. The plan calls for a four-part, phased-in implementation of decimal pricing with the first phase beginning on August 28, 2000 (this phase would consist of decimal pricing to begin in 13 exchange-listed securities and their options on August 28, 2000), and full implementation of decimal pricing for all equities and options on or before April 9, 2001. The plan is awaiting final approval from the SEC.

### Members' Decimalization Plans

Member firms are reminded to prepare a written decimalization plan. Each member firm should have a written plan that addresses its strategy for ensuring that it will be able to quote, trade, display, and store information in decimals. A decimalization plan should include, but not be limited to, the following:

1. An inventory and assessment of systems impacted by decimalization (both internal and external).  
**Recommended completion date: July 3, 2000.**
2. A remediation plan for those systems impacted by decimalization. Such remediation plans should address both decimal formatting as well as system processing capacity.  
**Recommended completion date: December 15, 2000.**
3. Testing plans (both internal and external). Again, such testing plans should address both decimal formatting as well as system processing capacity and should include participation in industry-wide testing if possible.  
**Recommended completion date: December 15, 2000.**
4. Verification of third-party vendor decimalization readiness (e.g., market data vendors, clearing agents, back-office systems, etc.).  
**Recommended completion date: December 15, 2000.**
5. Customer notification plans. This component should be an ongoing event.

This is a general outline of the basic expectation for members'

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decimalization plans; each member should consider the appropriate size, scope, and depth of its own decimalization plan. In addition, the recommended completion dates listed above are intended for member firms that are preparing for

Nasdaq decimalization. Member firms that participate in the intermarket (formerly known as the third market) should plan to prepare for the proposed phased-in period mentioned above which would begin on August 28, 2000.

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## INFORMATIONAL

### Interval Funds

NASD Adopts Exemption From The Corporate Financing Rule For Interval Funds; **Effective June 20, 2000**

## 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.*

- Corporate Finance
- Legal & Compliance
- Mutual Fund
- Registered Representatives

## KEY TOPICS

- Mutual Funds
- NASD Rule 2710
- NASD Rule 2830
- Underwriting Compensation

## Executive Summary

NASD Regulation, Inc. (NASD Regulation<sup>SM</sup>) has adopted amendments to National Association of Securities Dealers, Inc. (NASD<sup>®</sup>) Rules 2710 and 2830 to exempt certain closed-end mutual funds that are structured as "interval funds" from the filing requirements, filing fees, and regulations of Rule 2710 and instead to subject them to the Rule 2830, which regulates the distribution and sales charges of open-end funds.<sup>1</sup>

The text of the amendments is included with this *Notice to Members* (see Attachment A). The amendments became effective June 20, 2000.

## Questions/Further Information

Questions concerning this *Notice to Members* may be directed to Joseph E. Price, Director, Corporate Financing Department, NASD Regulation, at (240) 386-4623.

## Background

NASD Rule 2710 (Corporate Financing Rule) regulates the underwriting terms and other arrangements of public offerings of securities. Subparagraph (b)(8)(C) of the Corporate Financing Rule provides that offerings of securities of investment companies registered under the Investment Company Act of 1940 (1940 Act) are exempt from the Corporate Financing Rule, unless the offering is of securities of a management company defined as a "closed-end" company in Section 5(a)(2) of the 1940 Act (closed-end funds).<sup>2</sup> Thus, offerings of securities of closed-end funds are subject to the filing requirements, filing fees, and regulations of the Corporate Financing Rule. Continuous offerings of redeemable

securities of open-end investment management companies (open-end funds) are exempt from the Corporate Financing Rule. Instead, members' receipt of fees in connection with selling shares of open-end funds is regulated under NASD Conduct Rule 2830 (Sales Charge Rule).

The Corporate Financing Rule has long been applied to members' sales of the securities of closed-end funds on the basis that closed-end fund offerings are structured and marketed in a manner that is more similar to and competitive with corporate securities offerings than open-end funds. At the time the Corporate Financing Rule was adopted, closed-end funds conducted offerings of a fixed number of common shares at specified times; priced their shares periodically; limited sales compensation of broker/dealers to a discount from a fixed-offering price; did not redeem their securities; and generally listed their securities on a securities market.

## Interval Funds

Certain closed-end funds, commonly known as "interval funds," have developed a *hybrid* structure in which they engage in continuous offerings of their securities under Securities and Exchange Commission (SEC or Commission) Rule 415; price their shares daily; pay broker/dealers initial and continuing compensation that meets the limitations in the Sales Charge Rule; do not list their securities on a securities market; and redeem shares by making periodic self-tenders in compliance with Rule 23c-3(b) of the 1940 Act. Rule 23c-3(b) requires that interval funds establish a fundamental policy of making periodic repurchase offers; this policy is then changeable only by a majority

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vote of the outstanding voting securities of the company. Because the shares of interval funds are not redeemable on a daily basis, they are classified as "closed-end" under the 1940 Act.

NASD Regulation believes that the distribution of interval fund shares is conducted and financed in a manner more similar to that used by open-end funds than the method used by traditional closed-end funds. Therefore, the calculation of members' compensation for the distribution of interval fund shares is more properly regulated by the Sales Charge Rule, rather than by the limitations on underwriting compensation in the Corporate Financing Rule.

### Description Of Amendments

NASD Regulation has amended the Corporate Financing Rule and the Sales Charge Rule to exempt interval funds from the filing requirements, filing fees, and regulations of the Corporate Financing Rule and instead to subject them to the Sales Charge Rule, which regulates the distribution and sales charges of open-end funds.<sup>3</sup> The amendment to subparagraph (b)(8)(C) of the Corporate Financing Rule provides that closed-end fund offerings are exempt if the fund makes periodic

repurchase offers pursuant to Rule 23c-3(b) and it offers its shares on a continuous basis pursuant to Rule 415(a)(1)(xi) under the Securities Act of 1933. Closed-end funds that do not meet these requirements continue to be subject to the Corporate Financing Rule. The amendment to subparagraphs (d) and (j) of the Sales Charge Rule provide that interval funds are subject to the provisions regulating sales charges and the repurchases of fund securities.

### Implementation

The amendments became effective June 20, 2000. Interval funds that previously received a "no objections" opinion from the Corporate Financing Department based upon representations that underwriting compensation would not exceed the guidelines in the Corporate Financing Rule can now rely on the Sales Charge Rule limitations, provided that the Corporate Financing Rule's compensation limit has not already been met or exceeded. Any interval fund that has reached the applicable compensation limit under the Corporate Financing Rule shall remain subject to the requirements of this Rule until the fund files a post-effective amendment with the Commission registering additional securities.

### Endnotes

<sup>1</sup>Securities Exchange Act Release No. 42965 (June 20, 2000); 65 F.R. 39640 (June 27, 2000).

<sup>2</sup>Section 5(a)(1) of the 1940 Act defines "open-end company" as "a management company which is offering for sale or has outstanding any redeemable security for which it is the issuer." Section 5(a)(2) of the 1940 Act defines "closed-end company" as "any management company other than an open-end company."

<sup>3</sup>Interval funds are distinguished from other hybrid closed-end funds that make periodic self-tenders in compliance with Rule 13e-4 and Schedule 13E-4 under the Act ("tender offer funds"). Such tender offer funds are not required to establish as a fundamental policy that they will make periodic repurchases, as required by Rule 23c-3(b) under the 1940 Act. The rule change adopted herein would not exempt tender offer funds from the Corporate Financing Rule. However, NASD Regulation will consider individual requests for exemption under the Rule 9600 Series from the requirements of the Corporate Financing Rule for such tender offer funds. See, Exemption granted October 29, 1999 under "Corporate Financing Rule - Rule 2710" at the Exemption Requests Web Page on the NASD Regulation Web Site ([www.nasdr.com/2920.htm](http://www.nasdr.com/2920.htm)).

**ATTACHMENT A**

**Text Of Amendments**

*(Note: New text is underlined; deletions are bracketed.)*

**2710. Corporate Financing Rule - Underwriting Terms and Arrangements**

**(a)** No change

**(b) Filing Requirements**

**(1) – (7)** No change

**(8) Exempt Offerings**

Notwithstanding the provisions of subparagraph (1) above, the following offerings are exempt from this Rule, Rule 2720, and Rule 2810. Documents and information relating to the following offerings need not be filed for review:

**(A) – (B)** No change

**(C)** securities of [investment companies registered under the Investment Company Act of 1940, as amended, except securities of a management company defined as a “closed-end company” in Section 5(a)(2) of that Act] “open-end” investment companies as defined in Section 5(a)(1) of the Investment Company Act of 1940 and securities of any “closed-end” investment company as defined in Section 5(a)(2) of that Act that:

(i) make periodic repurchases offers pursuant to Rule 23c-3(b) under the Investment Company Act of 1940; and

(ii) offers its shares on a continuous basis pursuant to

Rule 415(a)(1)(xi) under the Securities Act of 1933.

**(D) – (J)** No change

**(9) – (12)** No change

**(c) – (d)** No change

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**2830. Investment Company Securities**

**(a) – (c)** No change

**(d) Sales Charge**

No member shall offer or sell the shares of any open-end investment company, any closed-end investment company that makes periodic repurchase offers pursuant to Rule 23c-3(b) under the 1940 Act and offers its shares on a continuous basis pursuant to Rule 415(a)(1)(xi) under the Securities Act of 1933, or any “single payment” investment plan issued by a unit investment trust (collectively “investment companies”) registered under the 1940 Act if the sales charges described in the prospectus are excessive. Aggregate sales charges shall be deemed excessive if they do not conform to the following provisions:

**(1) – (5)** No change

**(e) – (i)** No change

**(j) Repurchase from Dealer**

No member who is a principal underwriter of a security issued by an open-end [management] investment company or a closed-end investment company that makes periodic repurchase offers pursuant to Rule 23c-3(b) under the 1940 Act and offers its shares on a continuous basis pursuant to Rule

415(a)(1)(xi) under the Securities Act of 1933 shall repurchase such security, either as principal or as agent for the issuer, from a dealer acting as principal who is not a party to a sales agreement with a principal underwriter, nor from any investor, unless such dealer or investor is the record owner of the security so tendered for repurchase. No member who is a principal underwriter shall participate in the offering or in the sale of any such security if the issuer voluntarily redeems or repurchases its securities from a dealer acting as principal who is not a party to such a sales agreement nor from any investor, unless such dealer or investor is the record owner of the security so tendered for repurchase. Nothing in this paragraph shall relate to the compulsory redemption of any security upon presentation to the issuer pursuant to the terms of the security.

Nothing in this Rule shall prevent any member, whether or not a party to a sales agreement, from selling any such security for the account of a record owner to the underwriter or issuer at the bid price next quoted by or for the issuer and charging the investor to a reasonable charge for handling the transaction, provided that such member discloses to such record owner that direct redemption of the security can be accomplished by the record owner without incurring such charges.

**(k) – (n)** No change

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## INFORMATIONAL

# Ex-Dividend Dates

## NASD Reminds Members Of Methods For Determining Ex-Dividend Dates

### 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.*

- Legal & Compliance
- Registered Representatives
- Senior Management
- Trading & Market Making

### KEY TOPICS

- Ex-Dividend Dates

## Executive Summary

The National Association of Securities Dealers, Inc. (NASD<sup>®</sup>) Uniform Practice Code (UPC) governs, among other things, the designation of "ex-dividend dates" (ex-dates) for securities. The ex-date is the date on or after which a security is traded without a specific dividend or distribution. Under NASD rules, there are two different methods used to determine the ex-date of a security, depending upon the size of the dividend or distribution. This *Notice* reviews differences in the way ex-dates are determined and cautions members and their associated persons to be cognizant of these differences when providing ex-date information to customers.

## Questions/Further Information

Questions or comments concerning this *Notice* may be directed to Dorothy L. Kennedy, Director, Market Operations, The Nasdaq Stock Market, Inc. (The Nasdaq Stock Market<sup>®</sup>), at (203) 385-6243; and Shirley Weiss, Associate General Counsel, Office of General Counsel, NASD Regulation, Inc. (NASD Regulation<sup>SM</sup>), at (202) 728-8844.

## Background

NASD member firms or their registered representatives from time to time respond to customer inquiries regarding ex-dates relating to dividend and other distributions. In some cases, customers have drawn erroneous conclusions regarding ex-dates. In particular, large dividends that result in the designation of ex-dates *after* the record and payable dates have caused confusion in the case of customers who effect sales transactions after the record date but before the payable date and believe therefore that they are entitled to keep the dividend.

Securities and Exchange Commission (SEC) Rule 10b-17 requires issuers to give notice of dividends and distributions to the NASD no later than 10 days prior to the record date.<sup>1</sup> The NASD then establishes the ex-date for the distribution and makes this information publicly available on a Daily Dividend List on the Nasdaq Trader<sup>SM</sup> Web Site ([www.nasdaqtrader.com/dailylist/dl\\_di\\_ind.stm](http://www.nasdaqtrader.com/dailylist/dl_di_ind.stm)), which shows the issuer name and symbol, declaration date, amount of dividend, the ex-date, the record date, and the payable date.

## Determining The Ex-Date

UPC Rule 11140 governs the designation of ex-dates for securities. The ex-date is the date on or after which a security is traded without a specific dividend or distribution. The payable date is the date that the dividend is sent to the record owner of the security. Under the UPC, two methods are used to determine the ex-date of a security, depending on the size of the dividend or distribution.

### **Dividends Or Distributions Less Than 25 Percent Of Security Value**

The first method, under subparagraph(b)(1) of Rule 11140, provides that for dividends or distributions that are less than 25 percent of the value of the subject security, the date designated as the ex-date shall be the second business day preceding the record date. For example, if the issuer of the security has announced a date falling on a Thursday as the record date of a distribution, the ex-date will be on Tuesday, two days earlier. The price of the stock is adjusted downward on the ex-date so that the amount of the distribution is reflected in the current stock price. Thus, in this

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example, Tuesday is the day on or after which a buyer would purchase the security without the dividend and the seller of the security would keep the dividend. If the sale occurred on Monday, a day earlier, the seller would not keep the dividend.

### ***Dividends Or Distributions 25 Percent Or Greater Than Security Value***

The second method, under subparagraph (b)(2) of Rule 11140, provides that for dividends or distributions that are 25 percent or greater of the value of the subject security, the ex-date shall be the first business day following the payable date. For example, if an issuer has announced August 10 as the record date and August 31 as the payable date, then the ex-date will be September 1, the first

business day after the payable date. In this example, September 1 is the day on or after which a buyer would purchase the security without the dividend and, therefore, the day on which the price of the stock is adjusted downward. In this example, a seller of the security on August 15, even though the holder of record to receive the dividend, would have to relinquish the dividend to the buyer. Indeed, because the value of the security on August 15 has not yet been adjusted downward to reflect the dividend distribution, the seller in this example would be unjustly enriched by keeping the dividend. The seller would have received the value of the dividend twice: first, as fully reflected in the unadjusted price of the stock on August 15; and secondly, as subsequently paid by the company to record date holders.

This *Notice* reminds member firms and their associated persons that ex-dates are determined differently, depending on the size of the distribution. Current and historical dividend information is maintained by The Nasdaq Stock Market and can be found on the Nasdaq Trader Web Site at [www.nasdaqtrader.com/dailylist/dl\\_di\\_ind.stm](http://www.nasdaqtrader.com/dailylist/dl_di_ind.stm).

### **Endnote**

<sup>1</sup>The term "record date" under the Uniform Practice Code means the date fixed by the trustee, registrar, paying agent, or issuer for the purpose of determining the holders of equity securities, bonds, similar evidences of indebtedness, or unit investment trust securities entitled to receive dividends, interest or principal payments, or any other distributions.

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### INFORMATIONAL

## Arbitration Awards

NASD Dispute Resolution Will Require Firms To Certify In Writing That They Have Complied With Arbitration Awards Within 30 Days Of Receipt; **Effective Date: September 18, 2000**

### 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.*

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

### KEY TOPICS

- Arbitration Awards
- Motions To Vacate
- Nonpayment Of Awards
- Suspension Proceedings

### Executive Summary

To respond to concerns raised by the General Accounting Office, NASD Dispute Resolution, Inc. (formerly the Office of Dispute Resolution of NASD Regulation, Inc.) is implementing a system of monitoring and tracking compliance with arbitration awards by members and associated persons.

Starting on September 18, 2000, when claimants prevail in an arbitration proceeding, NASD Dispute Resolution will request to be notified by the claimants if a member or associated person has not paid the arbitration award within 30 calendar days of receipt of the award as required by Rule 10330(h). NASD Dispute Resolution will also require member firms to certify in writing that they have complied with awards against them or their associated persons.

### Questions/Further Information

Questions regarding this *Notice* may be directed to Jean I. Feeney, Special Advisor to the President, NASD Dispute Resolution, at (202) 728-6959 or via e-mail at: [jean.feeney@nasd.com](mailto:jean.feeney@nasd.com).

### Discussion

#### Background

On June 15, 2000, the United States General Accounting Office (GAO) issued a report entitled, *Securities Arbitration: Actions Needed to Address Problem of Unpaid Awards* (GAO Report).<sup>1</sup> The GAO Report was the culmination of an audit that began in the fall of 1998 and continued until the spring of 2000. GAO auditors surveyed 845 investors who received monetary awards in 1998 to determine how many awards had been paid or otherwise complied with. While the GAO Report found

that the NASD had initiated new arbitration processes to respond to recommendations contained in a 1992 GAO Report,<sup>2</sup> the GAO expressed concern that about 500 NASD awards to investors in 1998 either were unpaid or only partially paid.

The GAO observed that the NASD did follow up on all complaint letters it received concerning unpaid awards, and that most of the unpaid awards resulted from broker/dealers that were no longer in business. The GAO noted that, "Taking action to monitor the status of award payments and identify nonpaying brokers as soon as payment is due not only could benefit investors but also could help preserve their confidence in the arbitration process and thus benefit the entire securities industry."<sup>3</sup>

The GAO Report made several recommendations to deal with the problem of unpaid awards, including a recommendation that parties notify the NASD about the payment status of any monetary award when the 30-day payment period has passed. In response, NASD Dispute Resolution agreed to take appropriate measures to encourage prompt payment of arbitration awards. As part of those measures, NASD Dispute Resolution will now specifically request prevailing claimants to notify the forum in writing when their awards have not been paid, and will require member firms to certify in writing that they have complied with awards against them or their associated persons.<sup>4</sup>

Rule 10330(h) of the Code of Arbitration Procedure (Code) provides as follows:

All monetary awards shall be paid within thirty (30) days of receipt unless a motion to vacate

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has been filed with a court of competent jurisdiction. An award shall bear interest from the date of the award: (1) if not paid within thirty (30) days of receipt, (2) if the award is the subject of a motion to vacate which is denied, or (3) as specified by the arbitrator(s) in the award. Interest shall be assessed at the legal rate, if any, then prevailing in the state where the award was rendered, or at a rate set by the arbitrator(s).

The NASD By-Laws, Article VI, provide as follows:

### Sec. 3. Suspension or Cancellation of Membership or Registration

The NASD after 15 days notice in writing, may suspend or cancel the membership of any member or the registration of any person in arrears in the payment of any fees, dues, assessments, or other charges or for failure to furnish any information or reports requested pursuant to Section 2, or for failure to comply with an award of arbitrators properly rendered pursuant to the Rules of the Association, where a timely motion to vacate or modify such award has not been made pursuant to applicable law or where such a motion has been denied, or for failure to comply with a written and executed settlement agreement obtained in connection with an arbitration or mediation submitted for disposition pursuant to the Rules of the Association.

Therefore, if arbitration awards are not complied with in a timely manner, NASD Dispute Resolution currently institutes suspension proceedings against the member firm or associated person as provided in the NASD By-Laws and

the Rule 9510 Series, unless the member or associated person establishes one of the following bases for nonpayment, which are listed in the initial suspension warning letter:

1. The member or associated person made full payment of the award;
2. The parties have agreed to installment payments of the amount awarded or have otherwise agreed to settle the action;
3. The award has been modified or vacated by a court;
4. A motion to vacate or modify the award is pending in a court;<sup>5</sup> or,
5. The member or associated person has a bankruptcy petition pending in U.S. Bankruptcy Court pursuant to Title 11 of the United States Code (the Federal Bankruptcy Code), or the award in the action has been discharged by a U.S. Bankruptcy Court.

### New Notification Procedure

**For Claimants:** Beginning on September 18, 2000, letters to parties enclosing their arbitration awards will include a notice informing prevailing claimants that member firms and associated persons are required to comply with the award within 30 days of receipt unless they have a valid basis for not doing so, and that members and associated persons who do not comply with this requirement are subject to non-summary suspension proceedings. The notice will ask claimants to notify NASD Dispute Resolution in writing if their award has not been paid by the end of the 30-day period.

**For Respondents:** Letters enclosing arbitration awards in which the claimant has prevailed will include a notice requiring members to notify NASD Dispute Resolution in writing within 30 days of receipt if they or their associated persons have paid or otherwise complied with the award. If the member or associated person has not complied with the award, the member must identify a valid basis for nonpayment from among those listed above. This will enable NASD Dispute Resolution to institute suspension proceedings promptly when appropriate, and will prevent unnecessary regulatory effort in cases in which the award is the subject of a pending motion to vacate or there is another valid basis for nonpayment.

### Endnotes

<sup>1</sup>The GAO Report may be found on the Internet at: [www.gao.gov/new.items/gg00115.pdf](http://www.gao.gov/new.items/gg00115.pdf) or ordered through the Government Printing Office under the number GAO/GGD-00-115.

<sup>2</sup>That report was entitled *Securities Arbitration: How Investors Fare* (GAO/GGD-92-74, May 11, 1992).

<sup>3</sup>GAO Report at 38.

<sup>4</sup>Associated persons who have changed employment since the arbitration claim was filed will be required to notify NASD Dispute Resolution directly regarding the payment status of any awards against them.

<sup>5</sup>An award must be paid immediately when a court denies a motion to vacate or modify the award, absent a court order staying compliance with the award.

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**INFORMATIONAL**

**Code Of Procedure**

**SEC Approves Changes To Rule Regarding The Code Of Procedure**

**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.*

- Legal & Compliance
- Senior Management

**KEY TOPICS**

- Code Of Procedure
- Disciplinary Action Appeals
- Document Production
- Eligibility and Qualification Standards
- Failure to Respond
- Hearing Officers Authority
- Proceedings Imposing Limitations On Business Activities Re. Financial And/Or Operational Difficulties
- Statutory Disqualification

**Executive Summary**

On August 1, 2000, the Securities and Exchange Commission (SEC or Commission) approved rule changes proposed by the National Association of Securities Dealers, Inc. (NASD<sup>®</sup> or Association) that amend the NASD Code of Procedure (the Code) and other provisions to: set forth more clearly the Department of Market Regulation's role in disciplinary proceedings; clarify the authority of Hearing Officers and make some limited changes to that authority; clarify the scope of the Association's document production requirements; provide for hearing panel review of staff determinations to impose limitations on member firms' business activities because of financial and/or operational difficulties; provide for changes to the process for appeals of disciplinary actions, statutory disqualification proceedings, and certain other accelerated proceedings; provide for a streamlined process to impose bars or expulsions for the failure to provide information to the Association; and provide for a process by which the Association can more expeditiously cancel memberships of firms that fail to meet the Association's eligibility and qualification standards.

The rule changes are included with this *Notice* (see Attachment A). These changes become effective on September 11, 2000.

**Questions/Further Information**

Questions regarding this *Notice* may be directed to Eric Moss, Assistant General Counsel, Office of General Counsel, NASD Regulation, Inc. (NASD Regulation<sup>SM</sup>), at (202) 728-8982.

**Discussion**

The Code, implemented on August 7, 1997, provides detailed requirements governing NASD Regulation's process for:

- (1) authorizing, litigating, and issuing disciplinary decisions;
- (2) providing for appeals of those decisions;
- (3) taking certain actions through categories of accelerated proceedings; and
- (4) determining requests for relief from statutory disqualifications.

Since August 7, 1997, the Association staff has gained significant experience under the Code, and identified certain areas that need to be clarified or changed. On December 28, 1999, the Association proposed a series of clarifying and substantive amendments to the Code and other provisions as described below.<sup>1</sup> On May 10, 2000, the SEC published the NASD proposal for public comments,<sup>2</sup> and on August 1, 2000, the SEC issued an order approving these changes.<sup>3</sup>

***Custodian Of The Record***

Firms often list persons not associated with the firms as custodians of the record on SEC Form BDW, and then the Association may have difficulty obtaining records when firms no longer conduct business. NASD Rule 3121 was created to require members to designate, as the custodians of the record on Form BDW, persons who are associated with the firms at the time the forms are filed.

***Eligibility Of Panel Members***

In certain circumstances, the National Adjudicatory Council

(NAC) or the Review Subcommittee of the NAC (Review Subcommittee) may appoint panels to conduct hearings. Under Rule 1015, only one panel member can be from the NAC, unless a panel member is also a former NASD Regulation Director or NASD Governor. The Association believes that this unnecessarily limits the pool of potential panelists. The Association believes that members of the NAC possess specialized expertise that may not be fully utilized under the current rule language. Accordingly, the Association is eliminating this restriction.

### **Market Regulation's Role In Disciplinary Process**

Both the Department of Market Regulation and the Department of Enforcement represent NASD Regulation in formal disciplinary matters under the Code. However, the disciplinary rules only refer to the Department of Enforcement as the representative of the Association in these matters. The Department of Market Regulation also represents NASD Regulation under a delegation of authority from the Department of Enforcement, as stated in Rule 9120(e). The Association is amending the Code to clarify the Department of Market Regulation's role in the disciplinary process.

### **Investigations**

The Rule 8220 Series permits the Department of Enforcement to initiate proceedings, to suspend or cancel membership from the Association, or to suspend the association of a person with a member based upon the failure to provide information. These proceedings may be initiated for the failure to provide information pursuant to an Association request or the failure to make required filings with the Association, such as FOCUS reports, or failure to keep

the membership applications or supporting documents current. The Association is amending the Rule 8220 Series to:

- (1) as discussed below (under the heading *Failure To Respond*), limit the use of Rule 8220 Series proceedings to address the most serious ongoing violations concerning associated persons and members who fail to provide the Association with requested information; and
- (2) limit the sanctions available under Rule 8220 proceedings to suspensions.

Finally, the Association is amending the service provision under the Rule 8220 Series to make it consistent with the service provision under the Rule 9530 Series, a similar rule series. As modified, both the Rule 8220 Series and the Rule 9530 Series service provisions permit personal service, service by facsimile, and service by overnight courier. The Association is further clarifying that *attempted* delivery of a document by an overnight courier constitutes as service under these provisions.

### **Service Of Papers—Address Changes**

Rule 9134(b)(1) states that service of papers on a natural person in a disciplinary proceeding must be at the person's residential address as reflected in the Central Registration Depository (CRD<sup>SM</sup>). If the Association staff has actual knowledge that the person's residential CRD address is out of date, then in addition to serving at the residential address as reflected in the CRD, service should also be made at the person's last known residential address and the CRD address of the firm with which the person is associated or affiliated, if

he/she is currently in the industry. The Association is modifying the rule to permit adjudicators to waive the requirement of sending papers to CRD addresses when they are no longer valid, and when there is a more current address available. This change only relates to documents served on respondents after complaints have been served.

Further, the Association is amending Rule 9135(a) to clarify that complaints shall be deemed timely filed so long as they are either mailed or delivered to the Office of Hearing Officers within the two-year jurisdictional period, as outlined in the By-Laws.

### **Severance Of Cases**

Rule 9214 explicitly authorizes the Chief Hearing Officer to order the consolidation of disciplinary hearings, but does not discuss whether the Chief Hearing Officer has the authority to sever disciplinary proceedings. The Association is amending Rule 9214 to state that the Chief Hearing Officer has authority to sever disciplinary proceedings involving multiple respondents into two or more proceedings. Under the rule changes, the Chief Hearing Officer may order the severance of a disciplinary matter into two or more disciplinary proceedings, upon his or her own motion, or upon motion of a party. In determining whether to order the severance, the Chief Hearing Officer shall consider: (1) whether the same or similar evidence reasonably should be expected to be offered at each of the possible hearings; (2) whether the severance would conserve the time and resources of the parties; and (3) whether any unfair prejudice would be suffered by one or more of the parties if the severance is (not) ordered. If the Chief Hearing Officer issues an order to sever a disciplinary

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proceeding for which a hearing panel or extended hearing panel, if applicable, has been appointed, the Chief Hearing Officer's order shall specify whether the same hearing panel or extended hearing panel, if applicable, shall preside over the severed disciplinary proceedings, or shall appoint a new hearing panel(s) or extended hearing panel(s), if applicable, to preside over all severed proceedings, based on the criteria set forth in Rules 9231 and 9232.

### ***Producing Documents***

The Association is amending Rule 9253 to clarify the scope of the Association's document production requirements. Rule 9251(a) requires the Association staff to make available to respondents documents prepared or obtained by the staff in connection with the investigation that led to the institution of a disciplinary proceeding. Exceptions to the production requirements are listed in Rule 9251(b), and include examination and inspection reports and internal employee communications. Rule 9251(b) contains these exceptions because the materials listed in this provision often contain nonpublic information concerning the Association's investigative techniques. Notwithstanding these exceptions, such documents might become discoverable under Rule 9253 if staff members are called as witnesses during hearings. Rule 9253 requires Association staff to produce written statements made or adopted by staff members, if they relate to the subject matter of those persons' testimony. It also requires the staff to produce contemporaneously recorded recitals of oral statements made by witnesses, if those written statements are substantially verbatim.

The modifications of Rule 9253 clarify that the only portions of routine examination or inspection reports, internal employee communications, and any other internal documents that are required to be produced, under this rule, are the portions outlining the substance of (and any conclusions regarding) oral statements made by persons who are not employees of the Association when evidence of those statements is offered by Association staff during disciplinary hearings.

### ***Amending Complaints***

The Association is modifying its rules regarding amending complaints to more closely follow the Federal Rules of Civil Procedure (FRCP). The FRCP does not limit the types of amendments that may be made to complaints. NASD Rule 9212, however, only permits amendments to "new matters of fact or law." The Association is amending the rule to eliminate this restriction. Thus, for instance, under the rule change, the Association staff could amend complaints to include additional respondents.<sup>4</sup> Further, the FRCP permits amendments to make complaints conform to the evidence presented. The Association is modifying Rule 9212 to permit such amendments. Also, the FRCP states that amendments to complaints will be freely granted when justice so requires. The Association is amending Rule 9212 to state that amendments to complaints will be freely granted when justice so requires. Association staff will need to obtain Hearing Officer approval to amend complaints after answers have been filed.

### ***Effective Dates Of Sanctions***

CRD currently sets the effective dates of the imposition of sanctions imposed under the Code by notifying respondents in writing when fines are due and of the effective date of suspensions. The Association is amending Rules 9216, 9268, 9269, and 9360 to clarify that the effective dates of sanctions are the dates set by the Association staff unless stated otherwise in orders, decisions, or settlement agreements. As a result of these changes, the Association believes that IM-8310-2 is no longer needed, and accordingly, it is being deleted. This change will not effect the NASD's policy of automatically staying the imposition of the fines, disgorgement, and suspensions, pending appeal.

### ***Summary Dispositions***

Rule 9264(a) authorizes either the Association or respondents to file motions to summarily dispose of "any or all the causes of action in the complaint." This rule, however, does not permit parties to move to eliminate issues that do not involve entire "causes of actions." The Association is modifying Rule 9264(a) to track the language in the FRCP, which permits courts to dismiss issues.

Further, the Association is modifying Rule 9264 to authorize Hearing Officers to deny, grant, or defer motions to dismiss without referring the matter to the full panel. The authority to grant such motions would be limited to jurisdictional issues, such as whether the complaint was filed within the two-year jurisdictional period. The Association believes that Hearing Officers should be permitted to dismiss such motions which generally are technical legal questions.

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### ***Default Decisions***

Rule 9269 provides that motions to set aside default decisions should be made to the Review Subcommittee or the NAC. The Hearing Officers who issue the default decisions, however, are particularly familiar with the matters. The Association is modifying the rule to state that motions to set aside default decisions should be made to the Hearing Officers that originally decided the defaults. If the Hearing Officer that issued the original order is not available, the Chief Hearing Officer shall appoint another Hearing Officer to decide the motion. Appeals from such denials could be made to the NAC or the Review Subcommittee.

### ***Remand Cases***

Rule 9349 authorizes the NAC to remand disciplinary cases back to hearing panels. The Association is amending Rules 9344 and 9349 to clarify that the Review Subcommittee may also remand disciplinary cases back to hearing panels.

### ***Briefing Additional Issues On Appeal***

Currently, under Rule 9311 and Rule 9312, the General Counsel of NASD Regulation is required to obtain Review Subcommittee or NAC authorization to order parties to brief particular matters. The Association is modifying Rule 9311 and Rule 9312 to permit the General Counsel to order additional briefing without seeking the Review Subcommittee or the NAC authorization. Under this modified approach, parties may challenge, before the Review Subcommittee or the NAC, orders for additional briefing made by the General Counsel. Under the rule change, the hearing panels, once constituted by the NAC, will

continue to have the authority to order additional briefing.

### ***Briefing Schedules***

Rule 9347(b) establishes briefing schedules for papers filed in NAC proceedings. The Association is amending this rule to clarify that the time periods listed in the rule are only applicable to the principal briefing schedule and not applicable to the briefing of subsequent collateral issues.

### ***Procedures For Regulation Of Activities Of A Member Experiencing Financial Or Operational Difficulties***

Under the Rule 9410 Series, the Department of Member Regulation (Member Regulation) issues notices and holds initial hearings to determine whether members must limit their business activities as a result of financial and/or operational difficulties. Members can appeal Member Regulation's decisions to the NAC, and the NAC or the Review Subcommittee will appoint a subcommittee to participate in the review. The Association is amending the rule series to provide that firms may appeal limitations in notices issued by Member Regulation to hearing panels that will consist of a Hearing Officer and two other panelists. Under the change, Member Regulation would not hold hearings, and the NAC would not participate in matters handled under this rule series.

Currently, an NASD Governor may initiate the review of a decision issued by the NAC, under the Rule 9410 Series, not later than the next meeting of the NASD Board that is at least 15 days after the date on which the NASD Board receives the proposed written decision of the NAC. The Association is replacing this procedure with a mechanism by which the Executive Committee of the NASD Board may initiate the

review of the hearing panel decision not later than the next meeting of the Executive Committee that is at least 15 days after the date on which the Executive Committee receives the proposed written decision of the hearing panel. Currently, a decision issued by Member Regulation is stayed unless otherwise ordered by the NAC decision. The Association is modifying this provision to provide that Member Regulation's recommendation is stayed unless ordered otherwise by the Executive Committee.

### ***Other Proceedings***

Two categories of expedited proceedings available under the Rule 9510 Series are referred to as "summary proceedings" and "non-summary proceedings." The key differences between summary and non-summary proceedings are that: (1) in a summary proceeding, the Association can impose sanctions against a member or associated person before a hearing is held and a final Association decision is served, whereas in a non-summary proceeding, generally a hearing must be held and a final decision served before any sanction may be imposed; (2) a summary proceeding requires prior authorization by the NASD Board of Governors, whereas a non-summary proceeding may be initiated by staff without Board involvement; and (3) while the various forms of summary proceedings are enumerated in Section 15A(h)(3) of the Securities and Exchange Act of 1934, the other forms of expedited proceedings, including non-summary, are not.

The Association is making several amendments to the rules that govern the Code's summary and non-summary proceedings. Under the current rules, it is unclear as to

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whether Hearing Officers have all of the powers in summary and non-summary proceedings (the Rule 9500 Series) that they have in regular disciplinary proceedings (the Rule 9200 Series). The Association is adding a provision to the Rule 9500 Series stating that: "A Hearing Officer . . . shall have authority to do all things necessary and appropriate to discharge his or her duties as set forth under Rule 9235."

Rule 9514(a)(1) requires that requests for hearings be filed within seven days of receipt of suspension letters (or, with respect to notice of a pre-use filing requirement under Rule 2210(c)(4) and Rule 2220(c)(2), within 30 days of such notice). The Association is amending Rule 9514(a)(2) to clarify that if the member or person subject to the notice does not timely request a hearing under Rule 9514(a)(1), the notice shall constitute final Association action.

Rule 9514(d)(2) states that non-summary proceedings held under the Rule 9500 Series need to be held within 21 days after the respondent requests a hearing. Hearing panels may, during the initial 21-day periods, extend the time in which the hearings shall be held by additional 21-day periods. The Association believes that these periods are too short, and is amending the rule to extend the initial period to 40 days, with an additional 30 days of further extension. Since the suspension is not in effect during this time, this additional time will not prejudice respondents, and it will provide the staff and respondents with ample time to prepare for hearings.

Rule 9516 gives firms/persons suspended or limited under the Rule 9510 Series the opportunity to

become reinstated on the grounds of full compliance with the conditions of the suspension or limitation. The request needs to be filed with the department or office of the Association that acted as the party in the proceeding. If the department head denies reinstatement, the rule allows a party to file a request for relief with the NASD Board, and the NASD Board must respond in writing within 14 days. The Association believes that the matters appealed, however, do not require NASD Board review. The Association is changing the rule so that the appeals under Rule 9516 will be addressed by the Review Subcommittee of the NAC, rather than the NASD Board.

### ***Eligibility Proceedings***

The Association is making several changes to the Rule 9520 Series that governs the process by which persons may become or remain associated with a member notwithstanding the existence of a statutory disqualification or for a current member or person associated with a member to obtain relief from the eligibility or qualification requirements. First, the Rule 9520 Series does not state whether extensions of time or waivers of time limitations for filing of papers or holding of hearings may be granted. The Association is creating Rule 9524(a)(5) that permits such actions by consent of all the parties. Further, the eligibility rules do not state whether the disqualification hearing panel or the NAC may order that the record be supplemented. The Association is creating Rule 9524(a)(3)(c) to permit the hearing panel to order the parties to supplement the record with any additional evidence the hearing panel deems necessary.

Rule 9524(b)(3) states that NASD Regulation's statutory disqualification recommendations become effective upon service on applicants. However, only the denials are effective upon service on applicants (subject to the applicant requesting a stay of effectiveness from the SEC). Approval decisions are not effective until the Commission has either sent an acknowledgment letter to NASD Regulation (usually within 30 days, and the Commission can request a further 60-day extension of that period), or the Commission has entered an order in cases that have involved a previously entered Commission bar (there is no time limitation for the entry of such an order). The Association is amending this rule to reflect these points.

If a member files an application for relief under the eligibility rules, the NAC or the Review Subcommittee appoints a hearing panel composed of two or more members who are current or former members of the NAC or former Directors of NASD Regulation or Governors of the NASD. The Association is amending Rule 9524(a)(1) to state that current and former members of the Statutory Disqualification Committee may also serve on hearing panels.

Rule 9524(a)(3) states that if the Association staff initiated the proceedings, the Association will give to the applicant all documents that were relied on by the Association in issuing its notice. However, most applications are started by member firms, not the Association. The Association is amending this rule to reflect this fact.

The Association is also amending Rule 9524(a)(3) to provide that

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once an application is filed, CRD will gather all of the information necessary to process the application, including:

- (1) CRD records for the disqualified member, sponsoring member, and/or disqualified person, and the proposed supervisor; and
- (2) all of the information submitted by the disqualified member or sponsoring member in support of the application.

The revised Rule 9524(a)(3) will further provide that CRD will prepare an index of these documents, and simultaneously provide this index and copies of the documents to the disqualified member or sponsoring member, the NASD Regulation Office of General Counsel (Office of General Counsel), and Member Regulation. The rule also will require the Department of Member Regulation to submit its recommendation and supporting documents to the hearing panel and the disqualified member or sponsoring member within 10 business days of the hearing, unless the parties agree otherwise. Similarly, the disqualified member or sponsoring member will be required to submit its documents to the Office of General Counsel and Member Regulation within 10 business days of the hearing, unless agreed otherwise.

The amendments to the Rule 9520 Series also concern the review procedures undertaken by Association staff in the case of certain disqualifying events. In particular, the Association is amending Rule 9522(e) to permit members to submit a written request for relief (rather than an MC-400 application) in cases where

the disqualified member or person is subject to an injunction that was entered 10 or more years prior to the proposed admission or association. Under Exchange Act Rule 19h-1, the NASD is not required to provide any notice to the SEC of the proposed admission or association in these types of cases. The Association also made changes to enable members to file a written request for relief in cases where a member requests to change the supervisor of a disqualified person or where, for instance, the New York Stock Exchange has determined to approve the proposed association of a disqualified person and the NASD concurs with the determination. Member Regulation also will be granted discretion to approve the written request for relief in these cases, if it deemed such action to be consistent with the public interest and the protection of investors.

The Association also is amending the Rule 9520 Series to permit Member Regulation to approve an MC-400 application for relief in those cases where the disqualifying event is excepted from the "full" notice requirements of Rule 19h-1, but where a "short form" notification to the Commission under Rule 19h-1 is still required.<sup>5</sup> In these cases, the member would be required to file an MC-400, but Member Regulation would have the discretion to approve the application when consistent with the public interest and the protection of investors.

In addition, the Association is amending the Rule 9520 Series to create a more efficient mechanism to permit the membership or continued membership of a disqualified member or sponsoring

member, or the association or continuing association of a disqualified person, pursuant to an agreed-upon supervisory plan. The new procedures set forth in Rule 9523 are modeled on current Rule 9216 concerning Acceptance, Waiver, and Consent procedures, and are intended to avoid the requirement of a formal hearing and decision by the Statutory Disqualification Committee (and its hearing panels) in cases that generally involve only the issue of what type of supervisory plan is appropriate for the disqualified member or person. Under the revised Rule 9523, the member will still be required to file an MC-400 application with the NASD and Member Regulation will have the authority to recommend the approval or denial of the application. The new procedure, however, will permit the member to execute a letter consenting to the imposition of an agreed-upon supervisory plan. This letter and the agreed-upon supervisory plan will then be submitted to the Office of General Counsel for submission to the Chairman of the Statutory Disqualification Committee, acting on behalf of the NAC. The Chairman of the Statutory Disqualification Committee may accept or reject the recommendation of Member Regulation and the supervisory plan or refer them to the NAC for acceptance or rejection by the NAC. If the recommendation and supervisory plan is accepted by the NAC or the Chairman of the Statutory Disqualification Committee, it shall be deemed final. If the recommendation and supervisory plan are rejected either by the Chairman or the NAC, NASD Regulation may take any other appropriate action with respect to the disqualified member.

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### ***Failure To Respond***

As noted above (under the heading "Investigations"), proceedings initiated under the Rule 8220 Series are designed to address the most serious ongoing violations concerning associated persons and members that are failing to provide the Association with information.

The Association is creating a new rule series (Rule 9540 Series) which could be used against those who fail to provide the Association with information or required filings, or to keep membership applications or supporting documents current. Under the Rule 9540 Series, the Association would send notices informing respondents that failure to provide the Association with previously requested information or required filings or the failure to keep its membership application or supporting documents current will result in suspensions, unless the information is provided to the Association within 20 days. Respondents would have five days to request hearings to challenge proposed suspensions. Respondents who do not timely request hearings or timely provide requested information will be suspended. If a hearing is timely requested (within the five-day period) or otherwise requested within six months of the service of the notice, a respondent will

received a hearing conducted before a three-member hearing panel. The hearing panel would have the authority to order any fitting sanctions, including expulsion or bar. Respondents who fail to request hearings to challenge suspensions during the six-month period following the receipt of notices initiating proceedings under this rule series will be automatically barred or expelled.

### ***Proceeding For Failure To Meet Eligibility And Qualification Standards***

Further, the Association is including in the Rule 9540 Series a process by which Member Regulation could quickly cancel the memberships of firms that fail to meet the Association's eligibility and qualification standards. For instance, this new process could be used to cancel the membership of a firm that is not conducting a securities business (a By-Law eligibility/qualification requirement).

Pursuant to Rule 9540, the Association would send letters to members informing them that their memberships will be canceled within 20 days of receipt of the letters, unless the firm becomes eligible for continuance in membership within this time period. The members will be provided opportunities to request hearings

within five days of service of the notices to challenge the proposed cancellations. The hearings would be held before Hearing Officers.

### **Endnotes**

<sup>1</sup>File No. SR-NASD-99-76 (December 28, 1999), as amended by letter dated April 17, 2000.

<sup>2</sup>Release No. 42751 (May 3, 2000), 65 Fed. Reg. 30163 (May 10, 2000).

<sup>3</sup>Release No. 43102 (August 1, 2000), 65 Fed. Reg. 48266 (August 7, 2000).

<sup>4</sup>The Department of Market Regulation or the Department of Enforcement will seek authorization from the Office of Disciplinary Affairs before amending a complaint to include an additional respondent.

<sup>5</sup>"Short form notification" is required in the following situations: 1) the disqualified person has already been approved for association with a firm by a self-regulatory organization other than the Association; 2) the disqualified person has already been approved by the Association and the SEC for employment with a different member firm; and 3) the disqualification previously was a basis for the institution of an administrative proceeding pursuant to a provision of the federal securities laws, and was already considered by the Commission.

**ATTACHMENT A**

**Text Of Amendments**

*(Note: New text is underlined; deletions are bracketed.)*

\* \* \*

**1000. MEMBERSHIP, REGISTRATION AND QUALIFICATION REQUIREMENTS**

**1010. Membership Proceedings**

**1015. Review by National Adjudicatory Council**

(a) – (c) No Change

(d) Appointment of Subcommittee

The National Adjudicatory Council or the Review Subcommittee defined in Rule 9120 shall appoint a Subcommittee to participate in the review. The Subcommittee shall be composed of [at least two members. One member shall be a current member of the National Adjudicatory Council. The remaining member or members shall be current or past Directors or past Governors.] two or more persons who shall be current or past members of the National Adjudicatory Council or former Directors or Governors.

**3100. BOOKS AND RECORDS, AND FINANCIAL CONDITION**

**3121. Custodian of the Record**

A member who files a Securities and Exchange Commission Form BDW shall designate on the Form BDW, as the custodian of the record, a person associated with the member at the time that the Form BDW is filed.

**8000. INVESTIGATIONS AND SANCTIONS**

**8200. INVESTIGATIONS**

**8220. Suspension [or Cancellation] for Obstructing Investigations [Failure to Provide Requested Information]**

**8221. Notice**

(a) Notice to Member

If a member fails to provide any information, report, material, data, or testimony requested pursuant to the NASD By-Laws or the Rules of the Association[, or fails to keep its membership application or supporting documents current], the Department of Enforcement or the Department of Market Regulation may provide written notice to such member specifying the nature of the failure and stating that the failure to take such action within 20 days after service of the notice constitutes grounds for suspension [or cancellation] of membership.

(b) Notice to Person Associated with Member

If a person associated with a member fails to provide any information, report, material, data, or testimony requested pursuant to the NASD By-Laws or the Rules of the Association, the Department of Enforcement or the Department of Market Regulation may provide written notice to such person specifying the nature of the failure and stating that the failure to take such action within 20 days after service of the notice constitutes grounds for suspending the association of the person with the member.

(c) Service of Notice

The Department of Enforcement or the Department of Market Regulation shall serve the member or person associated with a member with such notice via personal service or overnight [commercial] courier or by facsimile at the location described in Rule 9134(b). Service by overnight courier shall be accomplished by sending the papers through an overnight courier service that generates a written confirmation of receipt or of attempts at delivery.

**8222. Hearing**

(a) Request for Hearing

Within five days after the date of service of a notice issued under Rule 8221, a member or person associated with a member served with a notice under Rule 8221(c) may file with the NASD Regulation Office of General Counsel a written request for an expedited hearing before a subcommittee of the National Adjudicatory Council. The request shall state with specificity why the member or associated person believes that there are insufficient grounds for suspension or [cancellation or] any other reason for setting aside the notice issued under Rule 8221.

(b) Hearing Procedures

(1) Appointment of Subcommittee

If a hearing is requested, the National Adjudicatory Council or the Review Subcommittee described in Rule 9120 shall appoint a subcommittee to conduct the hearing and decide whether the member or person associated with a member should be suspended [or canceled]. The subcommittee shall be composed of a current member of the National Adjudicatory Council

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and one or more current or former members of the National Adjudicatory Council[,] or former Governor or Director. [NASD Regulation Board, or NASD Board.]

### (2) Time of Hearing

The hearing shall be held within 30 days after the date of service of the notice issued under Rule 8221. Not later than seven days before the hearing, the subcommittee shall serve the member or person associated with a member with written notice of the date and time of the hearing via overnight [commercial] courier or facsimile and notify the Department of Enforcement or the Department of Market Regulation of the date and time of the hearing.

### (3) Transmission of Documents

Not later than seven days before the hearing, the Department of Enforcement or the Department of Market Regulation shall serve the member or person associated with a member via overnight [commercial] courier with all documents that were considered in connection with the decision to issue a notice under Rule 8221, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon the conclusion of any review by the Commission or the federal courts. The Department of Enforcement or the Department of Market Regulation shall provide a copy of the documents transmitted to the member or person

associated with a member to the subcommittee.

### (4) Counsel

The member or person associated with a member and the Department of Enforcement or the Department of Market Regulation may be represented by counsel at a hearing conducted under this Rule.

### (5) Evidence

Formal rules of evidence shall not apply to a hearing under this Rule. Not later than four days before the hearing, the member or person associated with a member and the Department of Enforcement or the Department of Market Regulation shall exchange copies of proposed hearing exhibits and witness lists and provide copies of the same to the subcommittee.

### (6) Witnesses – No Change

### (7) Additional Information

At any time during its consideration, the subcommittee may direct the member or person associated with a member or the Department of Enforcement or the Department of Market Regulation to submit additional information. Any additional information submitted shall be provided promptly to all parties at least one business day before the subcommittee renders its decision.

### (8) – (10) No Change

## 8223. Decision

### (a) Subcommittee

(1) Proposed Written Decision – No Change

### (2) Issuance of Decision After Expiration of Call for Review Period

If no Governor calls the proceeding for review within the time prescribed in paragraph (b)(1), the subcommittee's proposed written decision shall become final, and the subcommittee shall serve the final written decision on the member or associated person via overnight [commercial] courier or facsimile.

### (b) NASD Board of Governors

(1) Call For Review by Governor – No Change

### (2) Review and Decision

If a Governor calls the suspension [or cancellation] proceeding for review within the time prescribed in subparagraph (1), a review panel shall meet and conduct a review not later than 14 days after the call for review. The review panel shall be composed of the NASD Board Executive Committee, except that the Governor who calls the proceeding for review shall serve on the review panel in lieu of a member of the Executive Committee who has the same classification (Industry, Non-Industry, or Public) as such Governor. The review panel may affirm, modify, or reverse the decision of the subcommittee. Not later than seven days after the review panel meeting, the review panel shall serve a final written decision on the member or person associated with a member via overnight [commercial] courier or facsimile. The decision shall state the disposition of the suspension [or cancellation] proceeding, and if a suspension is imposed, state the

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grounds for the suspension and the conditions for terminating the suspension.

### 8225. Termination of Suspension

#### (a) Filing of Request

A suspended member or person associated with a member may file a written request for termination of the suspension on the ground of full compliance with the notice issued under Rule 8221 or, if applicable, the conditions of a decision under Rule 8223, with the head of the department or office of the Association that filed the notices under Rule 8221 [Department of Enforcement].

#### (b) Response by Association Staff [Department of Enforcement]

The head of the department of the Association that filed the notice under Rule 8221 [Department of Enforcement] shall respond to the request in writing within five days after receipt of the request.

#### (1) Request Granted

If the head of the department or office [Department of Enforcement] grants the request, he or she shall serve the member or person associated with a member with written notice of the termination of the suspension via overnight [commercial] courier or facsimile.

#### (2) Request Denied

If the head of the department or office denies the request, the suspended member or person associated with a member may file a written request for relief with the NASD Regulation Office of General Counsel. If the member or person associated

with a member files the written request for relief within 30 days after service of the decision under Rule 8223, the review panel constituted under Rule 8223 shall respond to the request for relief in writing within ten days after receipt of the request. If the member or person associated with a member files the written request for relief more than 30 days after service of the decision under Rule 8223, the National Adjudicatory Council shall respond to the request for relief in writing within ten days after receipt of the request. The review panel's or National Adjudicatory Council's response shall be served on the member or person associated with a member via overnight [commercial] courier or facsimile.

### 8300. SANCTIONS

#### 8310. Sanctions for Violation of the Rules

##### IM-8310-2. Release of Disciplinary Information

#### (a) – (b) No Change

(c) (1) The Association shall release to the public information with respect to any disciplinary complaint initiated by the Department of Enforcement or the Department of Market Regulation of NASD Regulation, Inc., the NASD Regulation, Inc. Board of Directors, or the NASD Board of Governors containing an allegation of a violation of a designated statute, rule or regulation of the Commission, NASD, or Municipal Securities Rulemaking Board, as determined by the NASD Regulation, Inc. Board of Directors (a "Designated Rule"); and may also release such

information with respect to any disciplinary complaint or group of disciplinary complaints that involve a significant policy or enforcement determination where the release of information is deemed by the President of NASD Regulation, Inc. to be in the public interest.

#### (2) No Change

#### (d) – (g) No Change

[(h) If a final decision of the Association is not appealed to the Commission, the sanctions specified in the decision (other than bars and expulsions) shall become effective on a date established by the Association but not before the expiration of 30 days after the date of the decision. Bars and expulsions, however, shall become effective upon issuance of the decision, unless the decision specifies otherwise.]

[(i)] [(i)] If a decision of the Association imposing monetary sanctions of \$10,000 or more or a penalty of expulsion, revocation, suspension and/or barring of a member from being associated with all members is appealed to the Commission, notice thereof shall be given to the membership and to the press as soon as possible after receipt by the Association of notice from the Commission of such appeal and the Association's notice shall state whether the effectiveness of the Board's decision has been stayed pending the outcome of proceedings before the Commission.

[(i)] [(j)] In the event an appeal to the courts is filed from a decision by the Commission in a case previously appealed to it from a decision of the Association, involving the imposition of monetary sanctions of \$10,000 or more or a penalty of

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expulsion, revocation, suspension and/or barring of a member from being associated with all members, notice thereof shall be given to the membership as soon as possible after receipt by the Association of a formal notice of appeal. Such notice shall include a statement whether the order of the Commission has been stayed.

(j)[(k)] Any order issued by the Commission of revocation or suspension of a member's broker/dealer registration with the Commission; or the suspension or expulsion of a member from the Association; or the suspension or barring of a member or person associated with a member from association with all broker/dealers or membership; or the imposition of monetary sanctions of \$10,000 or more shall be released to the public through a notice containing the effective date thereof sent as soon as possible after receipt by the Association of the order of the Commission.

(k)[(l)] Cancellations of membership or registration pursuant to the Association's By-Laws, Rules and Interpretative Material shall be released to the public as soon after the effective date of the cancellation as possible.

(l)[(m)] Releases to the public referred to in paragraphs (c) and (d) above shall identify the Rules and By-Laws of the Association or the SEC Rules violated, and shall describe the conduct constituting such violation. Releases may also identify the member with which an individual was associated at the time the violations occurred if such identification is determined by the Association to be in the public interest.

### 9000. CODE OF PROCEDURE

#### 9100. APPLICATION AND PURPOSE

#### 9120. Definitions

(a) – (d) No Change

(e) "Department of Enforcement"

The term "Department of Enforcement" means the Department of Enforcement of NASD Regulation [or its delegatee, the Department of Market Regulation].

(f) – (q) No Change

(r) "Interested Association Staff"

The term "Interested Association Staff" means, in the context of:

(1) a disciplinary proceeding under the Rule 9200 Series and the Rule 9300 Series:

(A) the Head of Enforcement;

(B) an employee of the Department of Enforcement who reports, directly or indirectly, to the Head of Enforcement;

(C) an Association employee who directly participated in the authorization of the complaint; [or]

(D) an Association employee who directly participated in an examination, investigation, prosecution, or litigation related to a specific disciplinary proceeding, and a district director or department head to whom such employee reports;

(E) the Head of the Department of Market Regulation; or

(F) an employee of the Department of Market Regulation who reports, directly or indirectly, to the Head of the Department of Market Regulation;

(2) – (4) No Change

(s) – (w) No Change

(x) "Party"

With respect to a particular proceeding, the term "Party" means:

(1) in the Rule 9200 Series and the Rule 9300 Series, the Department of Enforcement or the Department of Market Regulation or a Respondent;

(2) – (4) No Change

(y) – (bb) No Change

### 9130. Service; Filing of Papers

#### 9131. Service of Complaint and Document Initiating a Proceeding

(a) Service on Each Party

A complaint shall be served on each Party by the Department of Enforcement or the Department of Market Regulation. A document initiating a proceeding shall be served on each Party by the Party or person initiating such proceeding or his or her counsel or representative.

(b) – (c) No Change

#### 9134. Methods of, Procedures for Service

(a) Methods

(1) – (2) No Change

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### (3) Service by [Commercial] Courier

Service by [commercial] courier may be accomplished by sending the papers through a [commercial] courier service that generates a written confirmation of receipt or of attempts at delivery.

### (b) Procedures

#### (1) Service on Natural Persons

Papers served on a natural person may be served at the natural person's residential address, as reflected in the Central Registration Depository, if applicable. When a Party or other person responsible for serving such person has actual knowledge that the natural person's Central Registration Depository address is out of date, duplicate copies shall be served on the natural person at the natural person's last known residential address and the business address in the Central Registration Depository of the entity with which the natural person is employed or affiliated. Papers may also be served at the business address of the entity with which the natural person is employed or affiliated, as reflected in the Central Registration Depository, or at a business address, such as a branch office, at which the natural person is employed, or at which the natural person is physically present during a normal business day. The Hearing Officer may waive the requirement of serving documents (other than complaints) at the addresses listed in the Central Registration Depository if there is evidence that these addresses are no longer valid, and there is a more

current address available. If a natural person is represented by counsel or a representative, papers served on the natural person, excluding a complaint or a document initiating a proceeding, shall be served on the counsel or representative.

#### (2) No Change

#### (3) When Service Is Complete

Personal service and service by [commercial] courier or express delivery are complete upon delivery. Service by mail is complete upon mailing.

### 9135. Filing of Papers with Adjudicator: Procedure

#### (a) When to File

Papers that are required to be filed with an Adjudicator within a time limit specified by the Adjudicator or within a time limit set forth in the Rules shall be deemed timely if received within the time limit, unless otherwise ordered by an Adjudicator, except complaints, which shall be deemed timely filed upon mailing or delivery to the Office of Hearing Officers. Other papers that are required to be filed shall be deemed timely if, on the same day such papers are served, they are also hand-delivered, mailed via U.S. Postal service first class mail, or sent by courier to the Association.

#### (b) Where to File

All papers required to be filed pursuant to the Rule 9200 Series and any notice of appeal or review required to be filed pursuant to the Rule 9300 Series shall be filed with the Office of Hearing Officers. All other papers required to be filed pursuant to the Rule 9000 Series shall be filed where specified in the

Rule, or if not specified in the Rule, with the Adjudicator, unless the Adjudicator orders otherwise.

#### (c) Certificate of Service

Papers filed with an Adjudicator or the Office of Hearing Officers shall be accompanied by a certificate of service stating the name of the person or persons served, the date on which service is made, the method of service and, if service is not made in person, the address to which service is made. Such certificate shall be executed by the person who made the service. If the method of service on a Party is different from the method of service on any other Party, the certificate shall state why such different method was used.

### 9140. Proceedings

### 9146. Motions

#### (a) – (j) No Change

#### (k) Motion For Protective Order

(1) A Party, a person who is the owner, subject, or creator of a Document subject to production under Rule 8210 or any other Rule which may be introduced as evidence in a disciplinary proceeding, or a witness who testifies at a hearing in a disciplinary proceeding may file a motion requesting a protective order to limit disclosure or prohibit from disclosure to other Parties, witnesses or other persons, except the Department of Enforcement and the Department of Market Regulation and other Association staff, Documents or testimony that contain confidential information. The motion shall include a general summary or extract of the Documents or testimony without revealing confidential

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details. If the movant seeks a protective order against disclosure to other Parties, copies of the Documents shall not be served on the other Parties. Unless the Documents are unavailable, the movant shall file for in camera inspection a sealed copy of the Documents for which the order is sought. If the movant is not a Party, the motion shall be served on each Party by the movant using a method in Rule 9134(a) and filed with the Adjudicator. A motion for a protective order shall be granted only upon a finding that disclosure of the Document or testimony would have a demonstrated adverse business effect on the movant or would involve an unreasonable breach of the movant's personal privacy.

(2) No Change

(l) General – No Change

### 9200. DISCIPLINARY PROCEEDINGS

#### 9210. Complaint and Answer

#### 9211. Authorization of Complaint

(a) Complaint

(1) If the Department of Enforcement or the Department of Market Regulation believes that any NASD member or associated person is violating or has violated any rule, regulation, or statutory provision, including the federal securities laws and the regulations thereunder, which the Association has jurisdiction to enforce, the Department of Enforcement or the Department of Market Regulation may request authorization from the

Office of Disciplinary Affairs to issue a complaint.

(2) The NASD Regulation Board and the NASD Board each shall have the authority to direct the Office of Disciplinary Affairs to authorize and the Department of Enforcement or the Department of Market Regulation to issue a complaint when, on the basis of information and belief, either of such boards is of the opinion that any NASD member or associated person is violating or has violated any rule, regulation, or statutory provision, including the federal securities laws and the regulations thereunder, which the Association has jurisdiction to enforce.

(b) Commencement of Disciplinary Proceeding – No Change

#### 9212. Complaint Issuance — Requirements, Service, Amendment, Withdrawal, and Docketing

(a) Form, Content, Notice, Docketing, and Service

(1) If a complaint is authorized, the Department of Enforcement or the Department of Market Regulation shall issue the complaint. Each complaint shall be in writing and signed by the Department of Enforcement or the Department of Market Regulation. The complaint shall specify in reasonable detail the conduct alleged to constitute the violative activity and the rule, regulation, or statutory provision the Respondent is alleged to be violating or to have violated. If the complaint consists of several causes of action, each cause shall be stated separately. Complaints shall be served by the Department of Enforcement

or the Department of Market Regulation on each Party pursuant to Rules 9131 and 9134, and filed at the time of service with the Office of Hearing Officers pursuant to Rules 9135, 9136, and 9137.

(2) At the time of issuance of a complaint, the Department of Enforcement or the Department of Market Regulation may propose:

(A) an appropriate location for the hearing; and

(B) if the complaint alleges at least one cause of action involving a violation of a statute or a rule described in Rule 9120(s), that the Chief Hearing Officer select a Market Regulation Committee Panelist for the Hearing Panel, or, if applicable, the Extended Hearing Panel as described in Rule 9231.

(b) Amendments to Complaint

The Department of Enforcement or the Department of Market Regulation may file and serve an amended complaint [that includes new matters of fact or law] once as a matter of course at any time before the Respondent answers the complaint. Otherwise, upon motion by the Department of Enforcement or the Department of Market Regulation, the Hearing Officer may permit the Department of Enforcement or the Department of Market Regulation to amend the complaint, including amendments so as to make the complaint conform to the evidence presented [to include new matters of fact or law], after considering whether the Department of Enforcement or the Department of Market Regulation has shown good cause for the

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amendment and whether any Respondent will suffer any unfair prejudice if the amendment is allowed. Amendments to complaints will be freely granted when justice so requires.

### (c) Withdrawal of Complaint

With prior leave of the Hearing Officer, the Department of Enforcement or the Department of Market Regulation may withdraw a complaint. If the Department of Enforcement or the Department of Market Regulation withdraws the complaint before the earlier of (1) the Hearing Panel's or, if applicable, the Extended Hearing Panel's, issuance of a ruling on a motion for summary disposition, or (2) the start of the hearing on the merits, the withdrawal of the complaint by the Department of Enforcement or the Department of Market Regulation shall be without prejudice and the Department of Enforcement or the Department of Market Regulation shall be permitted to refile a case based on allegations concerning the same facts and circumstances that are set forth in the withdrawn complaint. If the Department of Enforcement or the Department of Market Regulation requests to withdraw such complaint after the occurrence of either of the two events set forth in (1) and (2) in this paragraph, the Hearing Panel or, if applicable, the Extended Hearing Panel, after considering the facts and circumstances of the request, shall determine whether the withdrawal shall be granted with prejudice.

### (d) Disciplinary Proceeding Docket – No Change

### 9213. Assignment of Hearing Officer and Appointment of Panelists to Hearing Panel or Extended Hearing Panel

#### (a) Assignment of Hearing Officer

As soon as practicable after the Department of Enforcement or the Department of Market Regulation has filed a complaint with the Office of Hearing Officers, the Chief Hearing Officer shall assign a Hearing Officer to preside over the disciplinary proceeding and shall serve the Parties with notice of the Hearing Officer's assignment pursuant to Rule 9132.

#### (b) Appointment of Panelists – No Change

### 9214. Consolidation or Severance of Disciplinary Proceedings

#### (a) Consolidation Initiated by Chief Hearing Officer

No Change

#### (b) Consolidation Initiated by a Party

No Change

#### (c) Impact on Hearing Panel or Extended Hearing Panel of Consolidation

No Change

#### (d) Severance Initiated by Chief Hearing Officer

The Chief Hearing Officer may order the severance of a disciplinary proceeding into two or more disciplinary proceedings, upon his or her own motion. In determining whether to order the severance of such disciplinary proceedings, the Chief Hearing Officer shall consider:

(1) whether the same or similar evidence reasonably would be expected to be offered at each of the possible hearings;

(2) whether the severance would conserve the time and resources of the Parties; and

(3) whether any unfair prejudice would be suffered by one or more Parties if the severance is (not) ordered.

If the Chief Hearing Officer proposes to sever a disciplinary proceeding, the Chief Hearing Officer shall serve upon the Parties notice of the proposed severance of disciplinary proceedings pursuant to Rule 9132. The Parties shall have 14 days after service to file a response, stating any arguments in favor of or opposition to severance.

#### (e) Severance Initiated by a Party

A Party may file a motion to sever a disciplinary proceeding if one or more of the factors favoring severance set forth in paragraph (d) appear to be present. If a Party moves to sever a disciplinary proceeding, the Party shall file such motion with the Office of Hearing Officers, and, pursuant to Rule 9133, shall serve the same upon each of the parties to the action proposed to be severed. The Parties shall have 14 days after service to file a response, stating any arguments in favor of or opposition to severance, and shall serve the response upon the Parties in the case proposed to be severed. The Chief Hearing Officer shall issue an order approving or denying the request for severance.

#### (f) Impact on Hearing Panel or Extended Hearing Panel of Severance

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If the Chief Hearing Officer issues an order to sever a disciplinary proceeding for which a Hearing Panel or, if applicable, Extended Hearing Panel, has been appointed, the Chief Hearing Officer's order shall specify whether the same Hearing Panel or, if applicable, Extended Hearing Panel, shall preside over the severed disciplinary proceedings, or shall appoint a new Hearing Panel(s) or, if applicable, Extended Hearing Panel(s), to preside over any or all of the severed proceedings, based on the criteria set forth in Rules 9231 and 9232.

### 9215. Answer to Complaint

(a) – (e) No Change

(f) Failure to Answer, Default

If a Respondent does not file an answer or make any other filing or request related to the complaint with the Office of Hearing Officers within the time required, the Department of Enforcement or the Department of Market Regulation shall send a second notice to such Respondent requiring an answer within 14 days after service of the second notice. The second notice shall state that failure of the Respondent to reply within the period specified shall allow the Hearing Officer, in the exercise of his or her discretion, pursuant to Rule 9269 to: (1) treat as admitted by the Respondent the allegations in the complaint; and (2) issue a default decision against the Respondent. If the Respondent fails to file an answer with the Office of Hearing Officers within the time required, the Hearing Officer may issue a default decision against the Respondent pursuant to Rule 9269.

### 9216. Acceptance, Waiver, and Consent; Plan Pursuant to SEC Rule 19d-1(c)(2)

(a) Acceptance, Waiver, and Consent Procedures

(1) Notwithstanding Rule 9211, if the Department of Enforcement or the Department of Market Regulation has reason to believe a violation has occurred and the member or associated person does not dispute the violation, the Department of Enforcement or the Department of Market Regulation may prepare and request that the member or associated person execute a letter accepting a finding of violation, consenting to the imposition of sanctions, and agreeing to waive such member's or associated person's right to a hearing before a Hearing Panel or, if applicable, an Extended Hearing Panel, and any right of appeal to the National Adjudicatory Council, the Commission, and the courts, or to otherwise challenge the validity of the letter, if the letter is accepted. The letter shall describe the act or practice engaged in or omitted, the rule, regulation, or statutory provision violated, and the sanction or sanctions to be imposed. Unless the letter states otherwise, the effective date of any sanction(s) imposed will be a date to be determined by the Association staff.

(2) – (4) No Change

(b) Procedure for Violation Under Plan Pursuant to SEC Rule 19d-1(c)(2)

(1) Notwithstanding Rule 9211, NASD Regulation or the National

Adjudicatory Council may, subject to the requirements set forth in subparagraphs (b)(2) through (b)(4) and in SEC Rule 19d-1(c)(2), impose a fine (not to exceed \$2,500) and/or a censure on any member or associated person with respect to any rule listed in IM-9216. If the Department of Enforcement or the Department of Market Regulation has reason to believe a violation has occurred and if the member or associated person does not dispute the violation, the Department of Enforcement or the Department of Market Regulation may prepare and request that the member or associated person execute a minor rule violation plan letter accepting a finding of violation, consenting to the imposition of sanctions, and agreeing to waive such member's or associated person's right to a hearing before a Hearing Panel or, if applicable, an Extended Hearing Panel, and any right of appeal to the National Adjudicatory Council, the Commission, and the courts, or to otherwise challenge the validity of the letter, if the letter is accepted. The letter shall describe the act or practice engaged in or omitted, the rule, regulation, or statutory provision violated, and the sanction or sanctions to be imposed. Unless the letter states otherwise, the effective date of any sanction(s) imposed will be a date to be determined by the Association staff.

(2) – (4) No Change

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### 9250. Discovery

### 9251. Inspection and Copying of Documents in Possession of Staff

(a) Documents to be Available for Inspection and Copying

(1) Unless otherwise provided by this Rule, or by order of the Hearing Officer, the Department of Enforcement or the Department of Market Regulation shall make available for inspection and copying by any Respondent, Documents prepared or obtained by Interested Association Staff in connection with the investigation that led to the institution of proceedings. Such Documents include but are not limited to:

(A) – (E) No Change

(2) The Department of Enforcement or the Department of Market Regulation shall promptly inform the Hearing Officer and each other Party if, after the issuance of a complaint, requests for information under Rule 8210 are issued under the same investigative file number under which the investigation leading to the institution of disciplinary proceedings was conducted. If Interested Association Staff receives Documents pursuant to a request for information under Rule 8210 after Documents have been made available to a Respondent for inspection and copying as set forth in paragraph (a), and if such Documents are material and relevant to the disciplinary proceeding in which such Respondent is a Party, the additional Documents shall be made available to the Respondent not later than 14 days after the Interested Association Staff receives such

Documents. If a hearing on the merits is scheduled to begin, Interested Association Staff shall make the additional Documents available to the Respondent not less than ten days before the hearing. If Interested Association Staff receives such Documents ten or fewer days before a hearing on the merits is scheduled to begin or after such hearing begins, Interested Association Staff shall make the additional Documents available immediately to the Respondent.

(3) Nothing in subparagraph (a)(1) shall limit the discretion of the Department of Enforcement or the Department of Market Regulation to make available any other Document or the authority of the Hearing Officer to order the production of any other Document.

(b) Documents That May Be Withheld

(1) The Department of Enforcement or the Department of Market Regulation may withhold a Document if:

(A) – (D) No Change

(2) Nothing in subparagraph (b)(1) authorizes the Department of Enforcement or the Department of Market Regulation to withhold a Document, or a part thereof, that contains material exculpatory evidence.

(c) Withheld Document List

The Hearing Officer may require the Department of Enforcement or the Department of Market Regulation to submit to the Hearing Officer a list of Documents withheld pursuant to subparagraphs (b)(1)(A) through (D) or to submit to the Hearing Officer any Document

withheld. Upon review, the Hearing Officer may order the Department of Enforcement or the Department of Market Regulation to make the list or any Document withheld available to the other Parties for inspection and copying. A motion to require the Department of Enforcement or the Department of Market Regulation to produce a list of Documents withheld pursuant to paragraph (b) shall be based upon some reason to believe that a Document is being withheld in violation of the Code.

(d) Timing of Inspection and Copying

The Hearing Officer shall determine the schedule of production of documents pursuant to this Rule. Unless otherwise ordered by the Hearing Officer, the Department of Enforcement or the Department of Market Regulation shall commence making Documents available to a Respondent for inspection and copying pursuant to this Rule not later than 21 days after service of the Respondent's answer or, if there are multiple Respondents, not later than 21 days after the last timely answer is filed. If a Respondent in a multi-Respondent case fails to answer, the Department of Enforcement or the Department of Market Regulation shall make Documents available to all other Respondents not later than the later of:

(1) 21 days after the filing date of the last timely answer, or

(2) the expiration of the second period provided for filing an answer as set forth in Rule 9215(f).

(e) – (f) No Change

(g) Failure to Make Documents Available — Harmless Error

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In the event that a Document required to be made available to a Respondent pursuant to this Rule is not made available by the Department of Enforcement or the Department of Market Regulation, no rehearing or amended decision of a proceeding already heard or decided shall be required unless the Respondent establishes that the failure to make the Document available was not harmless error. The Hearing Officer, or, upon appeal or review, a Subcommittee, an Extended Proceeding Committee, or the National Adjudicatory Council, shall determine whether the failure to make the document available was not harmless error, applying applicable Association, Commission, and federal judicial precedent.

### 9253. Production of Witness Statements

#### (a) Availability

Notwithstanding the provisions of Rule 9251(b),

(1) A Respondent in a disciplinary proceeding may file a motion requesting that the Department of Enforcement or the Department of Market Regulation produce for inspection and copying any statement of any person called or to be called as a witness by the Department of Enforcement or the Department of Market Regulation that pertains, or is expected to pertain, to his or her direct testimony and which is "a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement made by said witness and recorded contemporaneously with the making of such oral statement,"

as that phrase is used in 18 U.S.C. § 3500(e)(2).

(2) A Respondent in a disciplinary proceeding may also file a motion requesting that the Department of Enforcement or the Department of Market Regulation produce for inspection and copying any contemporaneously written statement made by an Interested Association Staff member during a routine examination or inspection about the substance of oral statements made by a non-Association person when (a) either the Interested Association Staff member or non-Association person is called as a witness by the Department of Enforcement or the Department of Market Regulation, and (b) that portion of the statement for which production is sought directly relates to the Interested Association Staff member's testimony or the testimony of the non-Association witness.

[A Respondent in a disciplinary proceeding may file a motion requesting that the Department of Enforcement produce for inspection and copying any statement of any person called or to be called as a witness by the Department of Enforcement that pertains, or is expected to pertain, to his or her direct testimony and that would be required to be produced pursuant to the Jencks Act, 18 U.S.C. § 3500. The production shall be made at a time and place fixed by the Hearing Officer and shall be made available to all Parties. Such production shall be made under conditions intended to preserve the items to be inspected or copied.]

(b) Failure to Produce — Harmless Error

In the event that a statement required to be made available for inspection and copying by a Respondent is not provided by the Department of Enforcement or the Department of Market Regulation, there shall be no rehearing of a proceeding already heard, or issuance of an amended decision in a proceeding already decided, unless the Respondent establishes that the failure to provide the statement was not harmless error. The Hearing Officer, or upon appeal or review, a Subcommittee, an Extended Proceeding Committee, or the National Adjudicatory Council, shall determine whether the failure to provide any statement was not harmless error, applying applicable Association, Commission, and federal judicial precedent.

### 9260. Hearing and Decision

### 9264. Motion for Summary Disposition

#### (a) Pre-hearing

After a Respondent's answer has been filed and Documents have been made available to that Respondent for inspection and copying pursuant to Rule 9251, the Respondent or the Department of Enforcement or the Department of Market Regulation, without leave of the Hearing Officer, may make a motion for summary disposition of any or all the causes of action in the complaint with respect to that Respondent, as well as any defense raised in a Respondent's answer. All pre-hearing motions for summary disposition and supporting papers shall be filed at least 21 days before the time set for the hearing, or at such earlier time as ordered by the Hearing Officer. Notwithstanding the provisions of Rule 9146(d), any opposition or response to a pre-hearing motion

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for summary disposition shall be filed at least seven days before the time set for the hearing.

### (b) After Commencement of Hearing on Merits

After a hearing on the merits has commenced, a Respondent or the Department of Enforcement or the Department of Market Regulation may make a motion for summary disposition of any or all of the causes of action in the complaint with respect to that Respondent or defenses raised in that Respondent's answer only with leave of the Hearing Officer.

### (c) Case Not Fully Adjudicated on Motion

If on motion under this rule a decision is not rendered upon the whole case or for all the relief asked and a hearing is necessary, the Hearing Panel or, if applicable, the Extended Hearing Panel, at the hearing of the motion, by examining the pleadings and the evidence before it and by questioning counsel, shall, if practicable, ascertain what material facts exist without substantial controversy and what material facts are actually and in good faith controverted. It shall thereupon make an order specifying the facts that appear without substantial controversy, and directing such further proceedings in the action as are just. Upon the hearing of the action the facts so specified shall be deemed established, and the hearing shall be conducted accordingly.

### (d) Form of Papers

A motion for summary disposition pursuant to paragraph (a) shall be accompanied by the following: a statement of undisputed facts; a supporting memorandum of points and authorities; and affidavits or

declarations that set forth such facts as would be admissible at the hearing and show affirmatively that the affiant is competent to testify to the matters stated therein. A memorandum of points and authorities in support or opposition shall not exceed 35 pages.

### (e) [(d)] Rulings on Motion

The Hearing Officer may promptly deny or defer decisions on any motion for summary disposition, however, only the Hearing Panel or, if applicable, the Extended Hearing Panel, may grant a motion for summary disposition, except the Hearing Officer may grant motions for summary disposition with respect to questions of jurisdiction.

[The Hearing Panel or, if applicable, the Extended Hearing Panel, shall promptly grant or deny the motion for summary disposition or shall defer decision on the motion.] The Hearing Panel or, if applicable, the Extended Hearing Panel, may grant the motion for summary disposition if there is no genuine issue with regard to any material fact and the Party that files the motion is entitled to summary disposition as a matter of law. If a Party files a motion under paragraph (a), the facts alleged in the pleadings of the Party against whom the motion is made shall be taken as true, except as modified by stipulations or admissions made by the non-moving Party, by uncontested affidavits or declarations, or by facts officially noticed pursuant to Rule 9145. If a Party opposing a motion for summary disposition made under paragraph (a) cannot present, by affidavit prior to the hearing, facts essential to justify the Party's opposition to the motion, the Hearing Panel or, if applicable, the Extended Hearing Panel, may deny the motion for summary disposition or defer the decision on the motion.

## 9268. Decision of Hearing Panel or Extended Hearing Panel

(a) Majority Decision – No Change

(b) Contents of Decision

The decision shall include:

(1) – (5) No Change

(6) a statement describing any sanction imposed, the reasons therefor, and the date upon which such sanction shall become effective. Unless otherwise provided in the decision, the sanction(s) shall become effective on a date to be determined by Association staff.

(c) – (e) No Change

## 9269. Default Decisions

(a) Issuance of Default Decisions

(1) No Change

(2) If the defaulting Party is the Respondent, the Hearing Officer may deem the allegations against that Respondent admitted. If the defaulting Party is the Department of Enforcement or the Department of Market Regulation, the Hearing Officer may issue a default decision ordering that the complaint be dismissed with prejudice.

(3) No Change

(b) Contents of Decision – No Change

(c) Review of Default Decision

Party may, for good cause shown, file a motion to set aside a default, dismissal, and the imposition of costs. Upon a showing of good cause, the Hearing Officer that entered the original order shall

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decide the motion. [either the Review Subcommittee or the National Adjudicatory Council may enter such an order.] If the Hearing Officer that issued the original order is not available, the Chief Hearing Officer shall appoint another Hearing Officer to decide the motion.

(d) Final Disciplinary Action of the Association; Effectiveness of Sanctions

If a default decision is not appealed pursuant to Rule 9311 or called for review pursuant to Rule 9312 within 25 days after the date the Office of Hearing Officers serves it on the Parties, the default decision shall become the final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1). Unless otherwise provided in the default decision, the sanction(s) shall become effective on a date to be determined by the Association staff [30 days after the default decision becomes the final disciplinary action of the Association], except that a bar or expulsion shall become effective immediately upon the default decision becoming the final disciplinary action of the Association. The Association shall serve the decision on a Respondent by [overnight] courier, facsimile or other means reasonably likely to obtain prompt service when the sanction is a bar or an expulsion.

### 9270. Settlement Procedure

(a) – (b) No Change

(c) Content and Signature Requirements

An offer of settlement shall be in writing and signed by the person making the offer, and, if the person

is represented by counsel or a representative, signed also by the counsel or representative. The offer of settlement shall contain in reasonable detail:

(1) – (3) No Change

(4) a statement consenting to findings of fact and violations consistent with the statements contained in the offer of settlement required by subparagraphs (c)(2) and (c)(3); [and,]

(5) a proposed sanction to be imposed that is consistent with the Association's then current sanction guidelines or, if inconsistent with the sanction guidelines, a detailed statement supporting the proposed sanction; and, [.]

(6) the effective date of any sanction(s) imposed, or a statement that the effective date of the sanction(s) will be a date to be determined by the Association staff.

(d) Waiver – No Change

(e) Uncontested Offers of Settlement

If a Respondent makes an offer of settlement and the Department of Enforcement or the Department of Market Regulation does not oppose it, the offer of settlement is uncontested. If an offer of settlement is determined to be uncontested by the Department of Enforcement or the Department of Market Regulation before a hearing on the merits has begun, the Department of Enforcement or the Department of Market Regulation shall transmit the uncontested offer of settlement and a proposed order of acceptance to the National

Adjudicatory Council with its recommendation. If an offer of settlement is determined to be uncontested by the Department of Enforcement or the Department of Market Regulation after a hearing on the merits has begun, the Department of Enforcement or the Department of Market Regulation shall transmit the offer of settlement and a proposed order of acceptance to the Hearing Panel or, if applicable, the Extended Hearing Panel for acceptance or rejection. If accepted by the Hearing Panel or, if applicable, Extended Hearing Panel, the offer of settlement and the order of acceptance shall be forwarded to the National Adjudicatory Council to accept or reject.

(1) – (3) No Change

(f) Contested Offers of Settlement

If a Respondent makes an offer of settlement and the Department of Enforcement or the Department of Market Regulation opposes it, the offer of settlement is contested. When the Department of Enforcement or the Department of Market Regulation opposes an offer of settlement, the Respondent's written offer and the Department of Enforcement's or the Department of Market Regulation's written opposition shall be submitted to a Hearing Panel or, if applicable, an Extended Hearing Panel. The Hearing Panel or, if applicable, the Extended Hearing Panel, may order the Department of Enforcement or the Department of Market Regulation and the Respondent to attend a settlement conference.

(1) – (3) No Change

(g) – (j) No Change

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### 9300. REVIEW OF DISCIPLINARY PROCEEDING BY NATIONAL ADJUDICATORY COUNCIL AND NASD BOARD; APPLICATION FOR COMMISSION REVIEW

### 9310. Appeal to or Review by National Adjudicatory Council

### 9311. Appeal by Any Party; Cross-Appeal

#### (a) Time to File Notice of Appeal

A Respondent or the Department of Enforcement or the Department of Market Regulation may file a written notice of appeal within 25 days after service of a decision issued pursuant to Rule 9268 or Rule 9269.

#### (b) – (d) No Change

#### (e) Waiver of Issues Not Raised

The National Adjudicatory Council may, in its discretion, deem waived any issue not raised in the notice of appeal or cross-appeal. The National Adjudicatory Council, the Review Subcommittee, a Subcommittee, the General Counsel or, if applicable, an Extended Proceeding Committee, [or, for a disciplinary proceeding decided under Rule 9269, the General Counsel,] shall provide the Parties with notice of, and an opportunity to submit briefs on, any issue that shall be considered by the National Adjudicatory Council if such issue was not previously set forth in the notice of appeal. Parties may submit motions to either the Review Subcommittee or the National Adjudicatory Council challenging requests for briefing made by the General Counsel under this Rule of issues that were not previously set forth in the notice of appeal.

(f) Withdrawal of Notice of Appeal or Cross-Appeal – No Change

### 9312. Review Proceeding Initiated By National Adjudicatory Council

#### (a) – (b) No Change

#### (c) Requirements

##### (1) No Change

(2) The statement contained in the notice of review shall not limit the scope of the National Adjudicatory Council's authority under Rule 9346 to review any issues raised in the record. The National Adjudicatory Council, the Review Subcommittee, a Subcommittee, the General Counsel or, if applicable, an Extended Proceeding Committee, [or, for a disciplinary proceeding decided under Rule 9269, the General Counsel] shall provide the Parties with notice of, and an opportunity to submit briefs on, any issue that shall be considered by the National Adjudicatory Council if such issue was not previously set forth in the notice of review. Parties may submit motions to either the Review Subcommittee or the National Adjudicatory Council challenging requests for briefing made by the General Counsel under this Rule of issues that were not previously set forth in the notice of appeal.

#### (d) Effect of Withdrawal of Notice of Appeal, Cross-Appeal

If the review of a disciplinary proceeding by the National Adjudicatory Council is terminated before the National Adjudicatory Council issues a decision on the merits because all appealing Parties file a notice of withdrawal of appeal and no Party previously filed

a notice of cross-appeal, or all Parties who previously filed a notice of cross-appeal file a notice of withdrawal of cross-appeal:

##### (1) No Change

(2) the General Counsel shall have the right to call for review a decision issued pursuant to Rule 9269 in accordance with Rule 9312(a)(2), except that the 25- [45] day period during which a call for review may be made shall begin on the day the Association receives the last filed notice of withdrawal of appeal or, if applicable, the last filed notice of withdrawal of cross-appeal.

### 9313. Counsel to National Adjudicatory Council

#### (a) Authority

[A Counsel to the National Adjudicatory Council shall be appointed by the General Counsel for each disciplinary case on appeal or review.] A Counsel to the National Adjudicatory Council shall have authority to take ministerial and administrative actions to further the efficient administration of a proceeding, including the authority to:

##### (1) – (7) No Change

#### (b) Review – No Change

### 9340. Proceedings

### 9344. Failure to Participate Below; Abandonment of Appeal

#### (a) Failure to Participate Below

When an appealing Party did not participate in the disciplinary proceeding before a Hearing Officer, a Hearing Panel or, if

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applicable, an Extended Hearing Panel, but shows good cause for the failure to participate, the National Adjudicatory Council or the Review Subcommittee may dismiss the appeal and remand the matter for further proceedings, or may order that the appeal proceed. If the appealing Party did not participate in the disciplinary proceeding before a Hearing Officer, a Hearing Panel or, if applicable, an Extended Hearing Panel, and fails to show good cause for the failure to participate, the matter shall be considered by the Subcommittee or, if applicable, the Extended Proceeding Committee, and the National Adjudicatory Council on the basis of the record and other documents, as provided in Rules 9346 and 9347. Alternatively, the National Adjudicatory Council or Review Subcommittee may remand the disciplinary proceeding with instructions. For purposes of this paragraph, failure to participate shall include failure to file an answer or otherwise respond to a complaint, or failure to appear at a scheduled hearing, but shall not include failure to request a hearing pursuant to Rule 9221.

(b) Abandonment of Appeal – No Change

### 9347. Filing of Papers in National Adjudicatory Council Proceedings

(a) Briefs; Reply Briefs; Requirements – No Change

(b) Timely Filing of Briefs

Briefs shall be due upon dates established by the Subcommittee or, if applicable, the Extended Proceeding Committee, the

National Adjudicatory Council, the Review Subcommittee, or Counsel to the National Adjudicatory Council in a scheduling order. Unless the Subcommittee or, if applicable, the Extended Proceeding Committee, the National Adjudicatory Council, the Review Subcommittee, or Counsel to the National Adjudicatory Council specifies otherwise, opening briefs shall be submitted not less than 21 days from the date of the scheduling order, and answering briefs shall be submitted 21 days thereafter. When reply briefs are submitted, such briefs shall be filed not later than ten days after service of the answering brief. Counsel to the National Adjudicatory Council may not shorten a period previously established for the filing of briefs except with the consent of the Parties. The time periods listed in this provision are only applicable to the filing of opening briefs, answering briefs, and reply briefs.

### 9349. National Adjudicatory Council Formal Consideration; Decision

(a) Decision of National Adjudicatory Council, Including Remand

In an appeal or review of a disciplinary proceeding governed by the Rule 9300 Series that is not withdrawn or dismissed prior to a decision on the merits, the National Adjudicatory Council, after considering all matters presented in the appeal or review and the written recommended decision of the Subcommittee or, if applicable, the Extended Proceeding Committee, may affirm, dismiss, modify or reverse the decision of the Hearing Panel or, if applicable, Extended

Hearing Panel, with respect to each Respondent who has appealed or cross-appealed or is subject to a call for review. The National Adjudicatory Council may affirm, modify, reverse, increase, or reduce any sanction, or impose any other fitting sanction. Alternatively, the National Adjudicatory Council or the Review Subcommittee may remand the disciplinary proceeding with instructions. The National Adjudicatory Council shall prepare a proposed written decision pursuant to paragraph (b).

(b) – (c) No Change

\* \* \*

### 9360. Effectiveness of Sanctions

Unless otherwise provided in the decision issued under Rule 9349 or Rule 9351, a sanction (other than a bar or an expulsion) specified in a decision constituting final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1) shall become effective on a date to be determined by Association staff [30 days after the date of service of the decision constituting final disciplinary action]. A bar or an expulsion shall become effective upon service of the decision constituting final disciplinary action of the Association [for purposes of SEC Rule 19d-1(c)(1)], unless otherwise specified therein. The Association shall serve the decision on a Respondent by [overnight] courier, facsimile or other means reasonably likely to obtain prompt service when the sanction is a bar or an expulsion.

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### 9400. LIMITATION PROCEDURES UNDER RULES 3130 AND 3131

#### 9410. Procedures for Regulating Activities of a Member Experiencing Financial or Operational Difficulties

#### 9412. Notice of Limitations

The Department of Member Regulation may issue a notice directing a member to limit its business activities if the Department of Member Regulation has reason to believe that any condition specified in Rule 3130 or 3131 exists. The notice shall specify the grounds on which such action is being taken, the nature of the limitations to be imposed, the effective date of the limitations, a fitting sanction that will be imposed if the member fails to comply with the limitations set forth in the notice, and the conditions for terminating such limitations. The effective date of the limitations shall be at least seven days after the date of service of the notice. The notice also shall inform the member that it may request a hearing before the Department of Member Regulation under Rule 9413. The Department of Member Regulation shall serve the notice by facsimile or overnight [commercial] courier.

#### 9413. [Department of Member Regulation Consideration

##### (a) Request for Hearing

A member aggrieved by a notice issued under Rule 9412 may file a written request for a hearing before the Department of Member Regulation. The request shall state the specific grounds for withdrawing or modifying the limitations specified in the notice. The request shall be filed pursuant to Rules

9135, 9136, and 9137 within five days after service of the notice under Rule 9412.

##### (b) Stay

A request for hearing shall stay the notice of limitations served under Rule 9412 unless the National Adjudicatory Council orders otherwise.

##### (c) Time of Hearing

If a member requests a hearing under paragraph (a), the Department of Member Regulation shall conduct a hearing within 14 days after service of the notice under Rule 9412. Not less than five business days before the hearing, the Department of Member Regulation shall provide written notice to the member of the location, date, and time of the hearing by facsimile or overnight commercial courier.

##### (d) Transmission of Documents

(1) Not less than five business days before the hearing, the Department of Member Regulation shall provide to the member by facsimile or overnight commercial courier all documents that were considered in imposing the limitations on business activities set forth in the notice served under Rule 9412, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon conclusion of any review by the Commission or the federal courts.

(2) Not less than five business

days before the hearing, the Department of Member Regulation and the member shall exchange proposed exhibit and witness lists. The exhibit and witness lists shall be served by facsimile or by overnight commercial courier.

##### (e) Hearing and Rights of Member

The member shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence. The hearing shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Department of Member Regulation within a reasonable time determined by the Department of Member Regulation. Upon notice to the participants in the hearing, the Department of Member Regulation may order corrections to the transcript as requested or sua sponte.

##### (f) Record

The record shall consist of:

(1) the notice issued pursuant to Rule 9412;

(2) all documents transmitted to the member under Rule 9413(d);

(3) the request for hearing filed pursuant to Rule 9413(a);

(4) any other submissions by the member and the Department of Member Regulation at the hearing;

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(5) any evidence considered at the hearing; and

(6) the transcript of the hearing and any corrections thereto.

(g) Custodian of the Record

The custodian of the record shall be the Department of Member Regulation.

(h) Evidence Not Admitted

Evidence that is proffered but not admitted during the hearing shall not be part of the record, but shall be retained by the custodian of the record until the date when the Association's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

(i) Decision

Within seven days after the hearing, the Department of Member Regulation shall issue a written decision approving, modifying, or withdrawing the limitations specified in the notice. If the decision imposes limitations, the decision shall state the grounds for the limitations, the conditions for terminating such limitations, and provide for a fitting sanction to be imposed under Rule 9416 if the member fails to comply with the limitations. The Department of Member Regulation shall promptly serve the decision by facsimile or overnight commercial courier. The limitations imposed shall become effective upon service of the decision.

(j) Failure to Request Hearing

If a member does not request a hearing under paragraph (a), the limitations specified in the notice shall become effective on the date specified in the notice. Unless the

National Adjudicatory Council calls the notice for review under Rule 9414(a)(2), the limitations specified in the notice shall remain in effect until the Department of Member Regulation reduces or removes the limitations pursuant to Rule 9417(b).]

### **[9414]. Hearing Panel Review [National Adjudicatory Council Review]**

[(a) Initiation of a Review]

(a)[(1)] Request for a Hearing [Application by Member]

A member subject [aggrieved] to [by] a notice [decision] issued under Rule 9412 [9413] may file a written request [application] for hearing [review by] before a Hearing Panel [the National Adjudicatory Council] with the Office of Hearing Officers. The request [application] shall state the specific grounds for withdrawing or modifying the limitations specified in the notice. The request shall be filed pursuant to Rules 9135, 9136, and 9137 within five days after service of the notice under Rule 9412. [the review and whether oral argument is requested. The application shall be filed pursuant to Rules 9135, 9136, and 9137 within seven days after service of the decision.] The member may withdraw its request [application for review] at any time by filing a written notice with the Office of Hearing Officers [National Adjudicatory Council] pursuant to Rules 9135, 9136, and 9137. The time limits set forth herein are to be strictly construed and cannot be modified except for good cause shown.

[(2) Motion of National Adjudicatory Council]

A decision issued under Rule 9413 shall subject to a call for

review by any member of National Adjudicatory Council or the Review Subcommittee within 30 days after service of the decision. If a member that receives a notice under Rule 9412 does not request a hearing under Rule 9413, the notice shall be subject to a call for review by any member of the National Adjudicatory Council or the Review Subcommittee within 30 days after the effective date of the notice. If the National Adjudicatory Council or the Review Subcommittee calls a decision or notice for review, a written notice of review shall be served promptly on the member pursuant to Rules 9132 and 9134. The notice of review shall state the specific grounds for the review and whether an oral argument is ordered. If a decision is called for review by a member of the National Adjudicatory Council or the Review Subcommittee, the National Adjudicatory Council shall review the decision.]

(b) Appointment of Hearing Panel

The Chief Hearing Officer shall assign a Hearing Officer to preside over the matter, and appoint Panelists pursuant to Rule 9231 and 9232 to the Hearing Panel. As soon as practicable after assignment, the Chief Hearing Officer shall serve the Parties with notice of the Hearing Panel.

(c)[(3)] Stay

Unless otherwise ordered by the NASD Board Executive Committee [National Adjudicatory Council], the initiation of a review under this paragraph shall stay the decision of the Department of Member Regulation or an uncontested notice until a decision constituting final action of the Association is issued.

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### (d)[(4)] Transmission of Documents [the Record]

(1) Not less than five business days before the hearing, the Department of Member Regulation shall file with the Office of Hearing Officers four copies of the record which shall consist of the notice issued under Rule 9412 and all correspondence between the Department of Member Regulation and the Member. The Department of Member Regulation shall simultaneously serve a copy of the record on the member by facsimile or overnight courier.

(2) Not less than five business days before the hearing, the Department of Member Regulation and the member shall exchange proposed exhibits and also exchange lists of all potential witnesses, including a brief description of the proposed testimony. The exhibits and the list of potential witnesses shall be served by facsimile or by overnight courier.

### (e) Time of Hearing

If a member requests a hearing under paragraph (a), the Hearing Panel shall conduct a hearing within 14 days after service of the notice under Rule 9412. Not less than five business days before the hearing, the Office of Hearing Officers shall provide written notice to the member of the location, date, and time of the hearing by facsimile or overnight courier.

### (f) Hearing and Rights of Member

The member shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence. The hearing shall be recorded and a transcript

prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Office of Hearing Officers within a reasonable time determined by the Office of Hearing Officers. Upon notice to the participants in the hearing, the Department of Member Regulation may order corrections to the transcript as requested or sua sponte.

### (g) Record of the Proceeding

The record shall consist of:

(1) the notice issued pursuant to Rule 9412;

(2) the request for hearing filed pursuant to Rule 9413;

(3) any other submissions by the member and the Department of Member Regulation at the hearing;

(4) any evidence considered at the hearing;

(5) the transcript of the hearing and any corrections thereto; and

(6) all documents transmitted to the member under Rule 9413(d).

### (h) Custodian of the Record

The custodian of the record shall be the Office of Hearing Officers.

### (i) Evidence Not Admitted

Evidence that is proffered but not admitted during the hearing shall not be part of the record, but shall be retained by the custodian of the record until the date when the

Association's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

[If a review is initiated under this paragraph, the Department of Member Regulation shall assemble and prepare an index of the record, transmit the record and index to the National Adjudicatory Council, certify to the National Adjudicatory Council that the record is complete, and serve a copy of the record and index on the member.]

### (j) Failure to Request Hearing

If a member does not request a hearing under paragraph (a), the limitations specified in the notice shall become effective on the date specified in the notice. Unless the Executive Committee calls the notice for review under Rule 9415, the limitations specified in the notice shall remain in effect until the Department of Member Regulation reduces or removes the limitations pursuant to Rule 9417(b).

### (k) Decision

(1) Within seven days after the hearing, the Hearing Panel shall issue a written decision approving, modifying, or withdrawing the limitations specified in the notice. If the decision imposes limitations, the decision shall state the grounds for the limitations, the conditions for terminating such limitations, and provide for a fitting sanction to be imposed under Rule 9416 if the member fails to comply with the limitations. The Office of Hearing Officers shall promptly serve the decision by facsimile or overnight courier pursuant to Rules 9132 and 9134. The limitations imposed shall become effective upon service of the decision.

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### (2) Contents of Decision

The decision shall include:

(A) a description of the Department of Member Regulation's decision, including its rationale;

(B) a description of the principal issues regarding the imposition of limitations raised in the review and a statement supporting the disposition of such issues;

(C) a summary of the evidence on each issue;

(D) a statement of whether the Department of Member Regulation's decision is affirmed, modified, or reversed, and a rationale therefor; and

(E) if any limitations are imposed:

(i) a description of the limitations and a statement describing a fitting sanction that will be imposed under Rule 9416 if the member fails to comply with any of the limitations; and

(ii) the conditions for terminating the limitations.

### (l) Issuance of Decision After Expiration of Call for Review Period

The Hearing Panel shall provide its proposed written decision to the NASD Board Executive Committee. The NASD Board Executive Committee may call the proceeding for review pursuant to Rule 9415. If the NASD Board Executive Committee does not call the proceeding for review, the proposed written decision of the Hearing Panel shall constitute the final action of the Association.

### (m)[(5)] Ex Parte Communications

The prohibitions against ex parte communications in Rule 9413 shall become effective under the Rule 9410 Series when Association staff has knowledge the NASD Board Executive Committee [National Adjudicatory Council] intends to review a decision on its own motion under this Rule.

### [(b) Subcommittee Consideration

#### (1) Appointment of Subcommittee

The National Adjudicatory Council or the Review Subcommittee shall appoint a Subcommittee to participate in the review. The Subcommittee shall be composed of two or more members. One member shall be a member of the National Adjudicatory Council, and the remaining member or members shall be current or former members of the National Adjudicatory Council or a former Director or Governor.

#### (2) Oral Argument

If oral argument is timely requested by the member, oral argument shall be held before the Subcommittee within 14 days after service of the decision under Rule 9413. If oral argument is ordered by the Subcommittee, oral argument shall be held before the Subcommittee within 14 days after service of the order under paragraph (a)(2). The member shall be entitled to be represented by an attorney. The oral argument shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of

his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Subcommittee within a reasonable time determined by the Subcommittee. Upon notice to the participants in the hearing, the Subcommittee may order corrections to the transcript as requested or sua sponte.

### (3) Review on Record

The Subcommittee shall conduct its review on the basis of the record, any written submissions by the member and the Department of Member Regulation, and the decision issued pursuant to Rule 9413(i). If oral argument is requested or ordered, Subcommittee also may consider any submissions or additional arguments by the member and the Department of Member Regulation.

### (4) Additional Evidence

The Subcommittee may consider any additional relevant and material evidence if the member shows good cause for not previously submitting such evidence. If additional evidence is accepted by the Subcommittee, the evidence shall be included in the record. Proffered evidence that is not accepted into the record by the Subcommittee shall be retained until the date when the Association's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

### (5) Recommendation

The Subcommittee shall present a recommended decision in writing to the National

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Adjudicatory Council not later than seven days before the meeting of the National Adjudicatory Council at which the proceeding shall be considered.

### (c) Decision

#### (1) Decision of National Adjudicatory Council, Including Remand

After considering all matters presented in the review and the written recommended decision of the Subcommittee, the National Adjudicatory Council may affirm, modify, or reverse the Department of Member Regulation's decision or remand the proceeding with instructions. The National Adjudicatory Council shall prepare a proposed written decision pursuant to subparagraph (2).

#### (2) Contents of Decision

The decision shall include:

(A) a description of the Department of Member Regulation's decision, including its rationale;

(B) a description of the principal issues regarding the imposition of limitations raised in the review and a statement supporting the disposition of such issues;

(C) a summary of the evidence on each issue;

(D) a statement of whether the Department of Member Regulation's decision is affirmed, modified, or reversed, and a rationale therefor; and

(E) if any limitations are imposed:

(i) a description of the limitations and a statement describing a fitting sanction that will be imposed under Rule 9416 if the member fails to comply with any of the limitations; and

(ii) the conditions for terminating the limitations.

#### (3) Issuance of Decision After Expiration of Call for Review Period

The National Adjudicatory Council shall provide its proposed written decision to the NASD Board. The NASD Board may call the proceeding for review pursuant to Rule 9415. If the NASD Board does not call the proceeding for review, the proposed written decision of National Adjudicatory Council shall become final, and the National Adjudicatory Council shall serve its written decision on the member and the Department of Member Regulation pursuant to Rules 9132 and 9134. The decision shall be effective upon service. The decision shall constitute the final action of the Association, unless National Adjudicatory Council remands the proceeding.]

### **9415. Discretionary Review by the NASD Board Executive Committee**

(a) Call for Review by NASD Board Executive Committee [Governor]

A member of the NASD Board Executive Committee [Governor] may call a proceeding for review by the NASD Board Executive Committee if the call for review is made within the period prescribed in paragraph (b).

(b) 15 Day Period; Waiver

A member of the NASD Board Executive Committee [Governor] shall make his or her call for review not later than the next meeting of the NASD Board Executive Committee that is at least 15 days after the date on which the NASD Board Executive Committee receives the proposed written decision of the Hearing Panel [National Adjudicatory Council]. By a unanimous vote of the NASD Board Executive Committee, the NASD Board Executive Committee may shorten the period to less than 15 days. By an affirmative vote of the majority of the NASD Board Executive Committee then in office, the NASD Board Executive Committee may, during the 15 day period, vote to extend the period to more than 15 days.

(c) Review at Next Meeting

If an NASD Board Executive Committee member [Governor] calls a proceeding for review within the period prescribed in paragraph (b), the NASD Board Executive Committee shall review the proceeding not later than the next meeting of the NASD Board Executive Committee. The NASD Board Executive Committee may order the filing of briefs in connection with its review proceedings pursuant to this Rule.

(d) Decision of NASD Board Executive Committee, Including Remand

After review, the NASD Board Executive Committee may affirm, modify, or reverse the proposed written decision of the Hearing Panel [National Adjudicatory Council]. Alternatively, the NASD Board Executive Committee may remand the proceeding with instructions. The NASD Board Executive Committee shall prepare

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a written decision that includes all of the elements described in Rule 9414(k)(2)(c)(2).

### (e) Issuance of Decision

The NASD Board Executive Committee shall issue and serve its written decision on the member and the Department of Member Regulation pursuant to Rules 9132 and 9134. The decision shall be effective upon service. The decision shall constitute the final action of the Association, unless the NASD Board Executive Committee remands the proceeding.

### 9416. Enforcement of Sanctions

#### (a) Order

If the Department of Member Regulation determines that a member has failed to comply with any limitations imposed by a decision or an effective notice under the Rule 9410 Series that has not been stayed, the Department of Member Regulation shall issue an order imposing the sanctions set forth in the decision or notice and specifying the effective date and time of such sanctions. The Department of Member Regulation shall serve the order on the member by facsimile or overnight [commercial] courier.

#### (b) Hearing

(1) A member subject to [aggrieved by] an order issued under paragraph (a) may file a written request for a hearing before a Hearing Panel with the Office of Hearing Officers [the Department of Member Regulation]. The request shall be filed pursuant to Rules 9135, 9136, and 9137 within seven days (including intermediate Saturdays, Sundays, and Federal

holidays) after service of the order. The Chief Hearing Officer shall assign a Hearing Officer to preside over the matter, and appoint Panelists pursuant to Rule 9231 and 9232 to the Hearing Panel. As soon as practicable after assignment, the Office of Hearing Officers shall serve the Parties with notice of the Hearing Panel. The hearing shall be held within ten days after service of the order under paragraph (a).

(2) The member shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence.

(3) The hearing shall be recorded and a transcript prepared by a court reporter. The member may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Office of Hearing Officers [Department of Member Regulation] within a reasonable time determined by the Office of Hearing Officers [Department of Member Regulation]. Upon notice to the participants in the hearing, the Office of Hearing Officers [Department of Member Regulation] may order corrections to the transcript as requested or sua sponte.

#### (c) No Stay of Sanctions

Unless otherwise ordered by the NASD Board Executive Committee [National Adjudicatory Council], a request for a hearing pursuant to this Rule shall not stay the effectiveness of the order issued under paragraph (a).

#### (d) Decision

Within four days after the hearing, the Hearing Panel [Department of Member Regulation] shall affirm, modify, or reverse the order issued under paragraph (a). The Office of Hearing Officers [Department of Member Regulation] shall serve the decision on the member pursuant to Rules 9132 and 9134. The decision shall become effective upon service and shall constitute final action of the Association.

## 9500. OTHER PROCEEDINGS

### 9510. Summary and Non-Summary Proceedings

#### 9512. Initiation of Summary Proceeding

##### (a) Authorization – No Change

##### (b) Contents and Service of Notice

A notice issued under this subsection shall state the specific grounds and include the factual basis for the summary suspension, limitation, or prohibition and state that the member, associated person, or other person may file a written request for a hearing under Rule 9514. The notice shall be served by facsimile or overnight [commercial] courier.

##### (c) Effective Date – No Change

### 9513. Initiation of Non-Summary Proceeding

#### (a) Notice

Association staff may initiate a proceeding authorized under Rule 9511(a)(2)(A) or (B), by issuing a written notice to the member, associated person, or other person. The notice shall specify the grounds for and effective date of

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the cancellation, suspension, bar, limitation, or prohibition and shall state that the member, associated person, or other person may file a written request for a hearing under Rule 9514. The notice shall be served by facsimile or overnight [commercial] courier.

(b) Effective Date – No Change

### 9514. Hearing and Decision

(a) Request

(1) Request by Member, Associated Person, or Other Person

No Change

(2) Failure to File Request

If the member, associated person, or other person subject to the notice issued under Rule 2210, 2220, 9512(a), or 9513(a) does not file a written request for a hearing within the time period specified in [under] subparagraph (1), the notice shall constitute final action by the Association.

(3) Ex Parte Communications – No Change

(b) Designation of Party for the Association and Appointment of Hearing Panel

If a member, associated person, or other person subject to a notice under Rule 2210, 2220, 9512, or 9513 files a written request for a hearing, an appropriate department or office of the Association shall be designated as a Party in the proceeding, and a Hearing Panel shall be appointed.

(1) – (2) No Change

(3) A Hearing Officer appointed pursuant to this provision shall

have authority to do all things necessary and appropriate to discharge his or her duties as set forth under Rule 9235.

(c) Stays – No Change

(d) Time of Hearing

(1) Summary Proceeding

If a member, associated person, or other person who is subject to a notice issued under Rule 9512(a) files a written request for a hearing, a hearing shall be held within seven days after the filing of the request for hearing. Not less than five days before the hearing, the Hearing Panel shall provide written notice to the Parties of the location, date, and time of the hearing by facsimile or overnight [commercial] courier.

(2) Non-Summary Proceeding

If a member, associated person, or other person who is subject to a notice issued under Rule 2210, 2220, or 9513(a) files a written request for a hearing, a hearing shall be held within 40 [21] days after the filing of the request for hearing. The Hearing Panel may, during the initial 40- [21] day period, extend the time in which the hearing shall be held by an additional 30 [21] days on its own motion or at the request of a Party. Not less than five days before the hearing, the Hearing Panel shall provide written notice to the Parties of the location, date, and time of the hearing by facsimile or overnight [commercial] courier.

(e) Transmission of Documents

(1) Not less than five days before the hearing, the Association shall provide to the member, associated person, or other

person who requested the hearing, by facsimile or overnight [commercial] courier, all documents that were considered in issuing the notice under Rule 2210, 2220, 9512, or 9513, unless a document meets the criteria of Rule 9251(b)(1)(A), (B), or (C). A document that meets such criteria shall not constitute part of the record, but shall be retained by the Association until the date upon which the Association serves a final decision or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

(2) Not less than five days before the hearing, the Parties shall exchange proposed exhibit and witness lists. The exhibit and witness lists shall be served by facsimile or by overnight [commercial] courier.

(f) Hearing Panel Consideration – No Change

### 9516. Reinstatement

A member, associated person, or other person who has been suspended or limited by a final action of the Association under the Rule 9510 Series may file a written request for reinstatement on the ground of full compliance with the conditions of the suspension or limitation. The request shall be filed with the department or office of the Association that acted as a Party in the proceeding. The head of the department or office shall serve its response on the member or person via facsimile or overnight [commercial] courier within five days after receipt of the request. If the head of the department or office denies the request, the member or person may file a written request for relief with the Review Subcommittee [NASD Board]. The

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Review Subcommittee [NASD Board] shall respond to the request in writing within 14 days after receipt of the request. The Review Subcommittee [NASD Board] shall serve its response by facsimile or overnight [commercial] courier.

### 9520. Eligibility Proceedings

#### 9521. Purpose and Definitions

##### (a) Purpose

The Rule 9520 Series sets forth procedures for a person to become or remain associated with a member, notwithstanding the existence of a [statutory] disqualification as defined in Article III, Section 4 of the NASD By-Laws [Section 3(a)(39) of the Act] and for a current member or person associated with a member to obtain relief from the eligibility or qualification requirements of the NASD By-Laws and the Rules of the Association. Such actions hereinafter are referred to as "eligibility proceedings."

##### (b) Definitions

(1) The term "Application" means NASD Regulation's Form MC-400 for individuals or Form MC-400A for members, filed with the Central Registration Depository/Public Disclosure.

(2) The term "disqualified member" means a broker, dealer, municipal securities broker or dealer, government securities broker or dealer, or member that is or becomes subject to a disqualification or is otherwise ineligible for membership under Article III, Section 3 of the NASD's By-Laws.

(3) The term "disqualified person" means an associated person or person seeking to become an

associated person who is or becomes subject to a disqualification or is otherwise ineligible for association under Article III, Section 3 of the NASD's By-Laws.

(4) The term "sponsoring member" means the member or applicant for membership pursuant to Rule 1013 that is sponsoring the association or continued association of a disqualified person to be admitted, readmitted, or permitted to continue in association.

#### 9522. Initiation of Eligibility Proceeding; Member Regulation Consideration

##### (a) Initiation by Association

(1) Issuance of Notice of Disqualification or Ineligibility

If Association staff has reason to believe that a [statutory] disqualification exists or that a member or person associated with a member otherwise fails to meet the eligibility requirements of the Association, Association staff shall issue a written notice to the member or applicant for membership under Rule 1013 [associated person]. The notice shall specify the grounds for such disqualification or ineligibility.

(2) Notice Regarding a [to] Member

A notice issued to a disqualified member [that is subject to a statutory disqualification or is otherwise ineligible for membership] shall state that the disqualified member may apply for relief by filing an [written] application [for relief pursuant to paragraph (c) with the National Adjudicatory Council] or, in the

case of a matter set forth in Rule 9522(e)(1), a written request for relief, within ten business days after service of the notice. If the member fails to file the [written] application [for relief] or, where appropriate, the written request for relief, within the 10-day period, the membership of the member shall be canceled, unless the Department of Member Regulation grants an extension for good cause shown.

(3) Notice Regarding an [to] Associated Person

A notice issued [to] regarding a[n] [associated] disqualified person [who is subject to a statutory disqualification or is otherwise ineligible for association] to a member or applicant for membership under Rule 1013 shall state that [a] such member or applicant for membership may file an application [apply for relief] on behalf of itself and such person [by filing a written application for relief pursuant to paragraph (c) with the National Adjudicatory Council] or, in the case of a matter set forth in Rule 9522(e)(1), a written request for relief, within ten business days after service of the notice. If the member fails to file the [written] application [for relief] or, where appropriate, the written request for relief, within the 10-day period, the registration of the [associated] disqualified person shall be revoked, unless the Department of Member Regulation grants an extension for good cause shown.

(4) Service

A notice issued under this section shall be served by facsimile or pursuant to Rules 9131 and 9134.

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### (b) Obligation of Member to Initiate Proceeding

A member shall file an [written] application [for relief from the eligibility requirements of the Association pursuant to paragraph (c) with the National Adjudicatory Council] or, in the case of a matter set forth in Rule 9522(e)(1), a written request for relief, with the Central Registration Depository/ Public Disclosure, if the member determines prior to receiving a notice under paragraph (a) that:

(1) it has become a disqualified member [the member is subject to a statutory disqualification or otherwise is no longer eligible for membership];

(2) a person associated with such member or whose association is proposed by an applicant for membership under Rule 1013 has become a disqualified person [is subject to a statutory disqualification or otherwise is no longer eligible for association with the member]; or

(3) the member or applicant for membership under Rule 1013 wishes to sponsor the association of a person who is a disqualified person. [subject to a statutory disqualification or otherwise is ineligible for association with a member.]

### [(c) Form of Application for Relief]

[A written application for relief shall be submitted on Form MC-400 and shall include a detailed statement demonstrating why the requested relief should be granted.]

### (c)[(d)] Withdrawal of Application

A member may withdraw its application or written request for relief prior to a hearing [at any time]

by filing a written notice with the [National Adjudicatory Council] Central Registration Depository/Public Disclosure pursuant to Rules 9135, 9136, and 9137. A member may withdraw its application after the start of a hearing but prior to the issuance of a decision by the National Adjudicatory Council with prior written consent of the National Adjudicatory Council.

### (d)[(e)] Ex Parte Communications

The prohibitions against ex parte communications set forth in Rule 9143 shall become effective under the Rule 9520 Series when Association staff has initiated the eligibility proceeding and Association staff has knowledge that a member intends to file an [written] application or written request for relief pursuant to the Rule 9520 Series [with the National Adjudicatory Council].

### (e) Member Regulation Consideration

(1) Matters that may be Approved by the Department of Member Regulation without the Filing of an Application

The Department of Member Regulation, as it deems consistent with the public interest and the protection of investors, may grant a written request for relief from the eligibility requirements by a disqualified member or a sponsoring member without the filing of an application by such disqualified member or sponsoring member if a disqualified member or disqualified person is subject to one or more of the following conditions but is not otherwise subject to disqualification:

(A) a disqualified member or

disqualified person is subject to a disqualification based on an injunction that was entered ten or more years prior to the proposed admission or continuance by order, judgment, or decree of any court of competent jurisdiction from acting as an investment adviser, underwriter, broker, dealer, municipal securities dealer, government securities broker, government securities dealer, transfer agent, foreign person performing a function substantially equivalent to any of the above, entity or person required to be registered under the Commodity Exchange Act, or any substantially equivalent foreign statute or regulation, or as an affiliated person or employee of any investment company, bank, insurance company, foreign entity substantially equivalent to any of the above, or entity or person required to be registered under the Commodity Exchange Act or any substantially equivalent foreign statute or regulation, or from engaging in or continuing any conduct or practice in connection with any such activity, or in connection with the purchase or sale of any security.

(B) a sponsoring member makes a request to change the supervisor of a disqualified person; or

(C) a disqualified member or sponsoring member is a member of both the Association and another self-regulatory organization; and:

(i) the other self-regulatory organization intends to file a Notice under SEC Rule 19h-1 approving the membership continuance of the

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disqualified member or, in the case of a sponsoring member, the proposed association or continued association of the disqualified person; and

(ii) Member Regulation concurs with that determination.

(2) Matters that may be Approved by the Department of Member Regulation after the Filing of an Application

The Department of Member Regulation, as it deems consistent with the public interest and the protection of investors, may approve an application filed by a disqualified member or sponsoring member if a disqualified member or disqualified person is subject to one or more of the following conditions but is not otherwise subject to disqualification (other than a matter set forth in subparagraph(e)(1)):

(A) The disqualified person is already a participant in, a member of, or a person associated with a member of, a self-regulatory organization (other than the Association), and the terms and conditions of the proposed admission to the Association are the same in all material respects as those imposed or not disapproved in connection with such person's prior admission or continuance pursuant to an order of the Commission under SEC Rule 19h-1 or other substantially equivalent written communication;

(B) The Department of Member Regulation finds, after reasonable inquiry, that except for the identity of the employer

concerned, the terms and conditions of the proposed admission or continuance are the same in all material respects as those imposed or not disapproved in connection with a prior admission or continuance of the disqualified person pursuant to an order of the Commission under SEC Rule 19h-1 or other substantially equivalent written communication, and that there is no intervening conduct or other circumstance that would cause the employment to be inconsistent with the public interest or the protection of investors; or

(C) The disqualification previously was a basis for the institution of an administrative proceeding pursuant to a provision of the federal securities laws, and was considered by the Commission in determining a sanction against such disqualified person in the proceeding; and the Commission concluded in such proceeding that it would not restrict or limit the future securities activities of such disqualified person in the capacity now proposed, or, if it imposed any such restrictions or limitations for a specified time period, such time period has elapsed.

(3) Rights of Disqualified Member, Sponsoring Member, Disqualified Person, and Department of Member Regulation

(A) In the event the Department of Member Regulation does not approve a written request for relief from the eligibility requirements pursuant to subparagraph (e)(1), the disqualified member or

sponsoring member may file an application, and such member shall have the right to proceed under Rule 9523 or 9524, as applicable. The Department of Member Regulation may require a disqualified member or sponsoring member to file an application with the Central Registration Depository/Public Disclosure, notwithstanding the provisions of subparagraph (e)(1).

(B) In the event the Department of Member Regulation does not approve an application pursuant to subparagraph (e)(2), the disqualified member or sponsoring member shall have the right to proceed under Rule 9523 or 9524, as applicable.

### **9523. Acceptance of Member Regulation Recommendations and Supervisory Plans by Consent Pursuant to SEC Rule 19h-1**

(a) After an application is filed, the Department of Member Regulation may recommend the membership or continued membership of a disqualified member or sponsoring member or the association or continuing association of a disqualified person pursuant to a supervisory plan where the disqualified member, sponsoring member, and/or disqualified person, as the case may be, consent to the recommendation and the imposition of the supervisory plan. The disqualified member, sponsoring member, and/or disqualified person, as the case may be, shall execute a letter consenting to the imposition of the supervisory plan.

(b)(1) If a disqualified member, sponsoring member, and/or disqualified person submitted an

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executed letter consenting to a supervisory plan, by the submission of such letter, the disqualified member, sponsoring member and/or disqualified person waive:

(A) the right to a hearing before a Hearing Panel and any right of appeal to the National Adjudicatory Council, the Commission, and the courts, or otherwise challenge the validity of the supervisory plan, if the supervisory plan is accepted.

(B) any right of the disqualified member, sponsoring member, and/or disqualified person to claim bias or prejudice by the Department of Member Regulation, the General Counsel, the National Adjudicatory Council, or any member of the National Adjudicatory Council, in connection with such person's or body's participation in discussions regarding the terms and conditions of the Department of Member Regulation's recommendation or the supervisory plan, or other consideration of the recommendation or supervisory plan, including acceptance or rejection of such recommendation or supervisory plan; and

(C) any right of the disqualified member, sponsoring member, and/or disqualified person to claim that a person violated the ex parte prohibitions of Rule 9143 or the separation of functions prohibitions of Rule 9144, in connection with such person's or body's participation in discussions regarding the terms and conditions of the recommendation or supervisory plan, or other consideration of the recommendation or supervisory plan, including acceptance or rejection of such

recommendation or supervisory plan.

(2) If a recommendation or supervisory plan is rejected, the disqualified member, sponsoring member, and/or disqualified person shall be bound by the waivers made under subparagraph (b)(1) for conduct by persons or bodies occurring during the period beginning on the date the supervisory plan was submitted and ending upon the rejection of the supervisory plan and shall have the right to proceed under this rule and Rule 9524, as applicable.

(c) If the disqualified member, sponsoring member, and/or disqualified person execute the letter consenting to the supervisory plan, it shall be submitted to the Office of General Counsel by the Department of Member Regulation with a proposed Notice under SEC Rule 19h-1, where required. The Office of General Counsel shall forward the supervisory plan and proposed Notice under SEC Rule 19h-1, if any, to the Chairman of the Statutory Disqualification Committee, acting on behalf of the National Adjudicatory Council. The Chairman of the Statutory Disqualification Committee may accept or reject the recommendation of the Department of Member Regulation and the supervisory plan or refer them to the National Adjudicatory Council for acceptance or rejection by the National Adjudicatory Council.

(d) If the recommendation and supervisory plan is accepted by the National Adjudicatory Council or the Chairman of the Statutory Disqualification Committee, it shall be deemed final and, where required, the proposed Notice under SEC Rule 19h-1 will be filed by the Association. If the

recommendation and supervisory plan are rejected by the Chairman of the Statutory Disqualification Committee or the National Adjudicatory Council, NASD Regulation may take any other appropriate action with respect to the disqualified member, sponsoring member, and/or disqualified person. If the recommendation and supervisory plan are rejected, the disqualified member, sponsoring member, and/or disqualified person shall not be prejudiced by the execution of the letter consenting to the supervisory plan under subparagraph (a) and the letter may not be introduced into evidence in any proceeding.

### **9524[9523]. National Adjudicatory Council Consideration**

(a) Hearing Panel Consideration

(1) Appointment of Hearing Panel

When the disqualified member, sponsoring firm, or applicant requests a hearing [If a member files an application for relief], the National Adjudicatory Council or the Review Subcommittee shall appoint a Hearing Panel composed of two or more members, who shall be current or former members of the National Adjudicatory Council or the Statutory Disqualification Committee or former Directors or Governors. The Hearing Panel shall conduct a hearing and recommend a decision on the request for relief.

(2) Notice of Hearing

The disqualified member or sponsoring member, as the case may be, and the Department of Member Regulation [Not less than fourteen days before the

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hearing, the member] shall be notified via mail, facsimile, or overnight [commercial] courier of the location, time, and date of the hearing not less than fourteen business days before the hearing, unless the parties agree to shorten the time period.

### (3) Transmission of Documents

(A) Upon receipt of an application, the Central Registration Depository shall gather all of the information necessary to process the application, including (i) the Central Registration Depository records for the disqualified member, sponsoring member, and/or disqualified person, as the case may be, and the proposed supervisor; and (ii) all of the information submitted by the disqualified member or sponsoring member in support of the application. The Central Registration Depository will prepare an index of these documents, and simultaneously provide this index and copies of the documents to the disqualified member or sponsoring member, as the case may be, the Office of the General Counsel, and the Department of Member Regulation. [If Association staff initiated the eligibility proceeding by issuing a notice under Rule 9522(a), Association staff shall provide to the member and its current or prospective associated person all documents that were relied on in issuing the notice.] Such documents shall be served on the disqualified member [and its current or prospective associated person] or sponsoring member, as the case may be, by mail, facsimile, or overnight [commercial] courier as soon as practicable

[not less than ten days before the hearing]. The Department of Member Regulation shall serve its recommendation and its supporting documents on the Office of General Counsel and the disqualified member or sponsoring member, as the case may be, within ten business days of the hearing, unless the Parties agree otherwise. The disqualified member or sponsoring member, as the case may be, shall serve its documents on the Office of General Counsel and the Department of Member Regulation within ten business days of the hearing, unless the Parties agree otherwise. The Office of General Counsel shall forward all documents transmitted to it pursuant to this subparagraph (a)(3) to the Hearing Panel.

(B) Not less than ten business days before the hearing, the Department of Member Regulation, which shall act as a Party in the eligibility proceeding, and the disqualified member [and its current or prospective associated person] or sponsoring member, as the case may be, shall [exchange] serve proposed exhibit and witness lists on each other and the Office of General Counsel. The exhibit and witness lists shall be served by facsimile or overnight [commercial] courier.

(C) At any time prior to the issuance of its recommendation, the Hearing Panel may order the Parties to supplement the record with any additional information that the Hearing Panel deems necessary.

(4) Rights of Disqualified Member, Sponsoring Member, Disqualified [Current or

Prospective Associated] Person, and Department of Member Regulation

The disqualified member, sponsoring member, [its current or prospective associated] and/or disqualified person, as the case may be, and, the Department of Member Regulation, shall be entitled to be heard in person, to be represented by an attorney, and to submit any relevant evidence.

(5) Extensions of Time, Postponements, and Adjournments

At any time prior to the issuance of the decision of the Hearing Panel, after obtaining consent of all the Parties, the Hearing Panel may extend or shorten any time limits prescribed by the Code for the filing of any papers and may postpone or adjourn any hearing.

(6)[(5)] Recordation of Hearing

The hearing shall be recorded and a transcript prepared by a court reporter. The disqualified member, sponsoring member, and/or [the current or prospective associated] disqualified person, as the case may be, may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Hearing Panel within a reasonable time determined by the Hearing Panel. Upon notice to the participants in the hearing, the Hearing Panel may order corrections to the transcript as requested or sua sponte.

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### (7)(6) Record

The record shall consist of:

- (A) the notice issued pursuant to Rule 9522(a), if applicable;
- (B) all documents relied upon in issuing the notice under Rule 9522(a), if applicable;
- (C) the application for relief filed pursuant to Rule 9522(b);
- (D) any other submissions by the disqualified member, sponsoring member, and/or [the] [current or prospective associated] disqualified person, as the case may be, and the Department of Member Regulation;
- (E) any evidence considered at the hearing; and
- (F) the transcript of the hearing and any corrections thereto.

### (8)(7) Custodian of the Record

The custodian of the record shall be the Office of General Counsel of NASD Regulation.

### (9)(8) Evidence Not Admitted

Evidence that is proffered but not admitted during the hearing shall not be part of the record, but shall be retained by the custodian of the record until the date when the Association's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

### (10)(9) Recommendation

On the basis of the record, the Hearing Panel shall present a recommended decision in writing on the request for relief to the

Statutory Disqualification Committee. After considering the record and recommendation of the Hearing Panel, the Statutory Disqualification Committee shall present its recommended decision in writing to the National Adjudicatory Council [not later than seven days before the meeting of the National Adjudicatory Council at which the eligibility proceeding shall be considered].

### (b) Decision

#### (1) Decision of the National Adjudicatory Council

After considering all matters presented in the request for relief, the Statutory Disqualification Committee's recommended decision, the public interest, and the protection of investors, the National Adjudicatory Council may grant or deny the request for relief, and, if relief is granted, impose conditions on the disqualified member, sponsoring member, and/or [its current or prospective associated] disqualified person, as the case may be. At any time prior to the issuance of its recommendation, the National Adjudicatory Council may order the Parties to supplement the record with any additional information that the National Adjudicatory Council deems necessary. Alternatively, the National Adjudicatory Council may remand the eligibility proceeding. The National Adjudicatory Council shall prepare a proposed written decision pursuant to subparagraph (2).

#### (2) Contents of Decision

The decision shall include:

(A) No Change

(B) No Change

(C) a statement in support of the disposition of the request for relief, which, if granted, includes any of the applicable elements under SEC Rule 19h-1(e) and a description of any conditions that are imposed on the disqualified member, sponsoring member, or disqualified [and current or prospective associated] person, as the case may be.

#### (3) Issuance of Decision After Expiration of Call for Review Period

The National Adjudicatory Council shall provide its proposed written decision to the NASD Board. The NASD Board may call the eligibility proceeding for review pursuant to Rule 9525 [9524]. If the NASD Board does not call the eligibility proceeding for review, the proposed written decision of the National Adjudicatory Council shall become final, and the National Adjudicatory Council shall serve its written decision on the disqualified member, sponsoring member, and/or [the current or prospective associated] disqualified person, as the case may be, and the Department of Member Regulation pursuant to Rules 9132 and 9134. [The decision shall be effective upon service.] The decision shall constitute final action of the Association, unless the National Adjudicatory Council remands the eligibility proceeding. A decision to deny re-entry or continued association shall be effective immediately. A decision to approve shall be effective after the Commission issues an acknowledgment letter or, in

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cases involving Commission ordered sanctions, an order.

### **9525[9524]. Discretionary Review by the NASD Board**

(a) – (c) No Change

(d) Decision of NASD Board, Including Remand

After review, the NASD Board may affirm, modify, or reverse the proposed written decision of the National Adjudicatory Council. Alternatively, the NASD Board may remand the eligibility proceeding with instructions. The NASD Board shall prepare a written decision that includes all of the elements described in Rule 9524(b)(2) [9523(b)(2)].

(e) Issuance of Decision

The NASD Board shall issue and serve its written decision on the disqualified member, sponsoring member, and/or disqualified [the current or prospective associated] person, as the case may be, and the Department of Member Regulation pursuant to Rules 9132 and 9134. The decision shall [be effective upon service. The decision shall] constitute the final action of the Association, unless the NASD Board remands the proceeding. A decision to deny re-entry or continued association shall be effective immediately. A decision to approve shall be effective after the Commission issues an acknowledgment letter or, in cases involving Commission-ordered sanctions, an order.

### **9526[9525]. Expedited Review**

(a) Direction by Executive Committee

Notwithstanding Rules [9523 and] 9524 and 9525, the NASD Board

Executive Committee, upon request of the Statutory Disqualification Committee, may direct an expedited review of a recommended written decision of the Statutory Disqualification Committee if the NASD Board Executive Committee determines that expedited review is necessary for the protection of investors.

(b) Call for Review Period – No Change

(c) No Call for Review

If no Governor calls the proceeding for review within the time prescribed, the decision shall become final, and the Statutory Disqualification Committee shall serve the decision on the disqualified member, sponsoring member, and/or disqualified [the current or prospective associated] person, as the case may be, and the Department of Member Regulation pursuant to Rules 9132 and 9134. The decision shall [be effective upon service and shall] constitute final action of the Association. The decision shall be effective upon approval by the Commission.

(d) Call for Review

If a Governor calls the eligibility proceeding for review within the prescribed time, a review panel shall meet and conduct a review not later than 14 days after the call for review. The review panel shall be composed of the NASD Board Executive Committee, except that the Governor who calls the proceeding for review shall serve on the review panel in lieu of a member of the Executive Committee who has the same classification (Industry, Non-Industry, or Public) as such Governor. The review panel may affirm, modify, or reverse the

recommended written decision of the Statutory Disqualification Committee or remand the eligibility proceeding with instructions. The review panel shall prepare, issue, and serve its decision pursuant to Rule [9524] 9525(d) and (e).

### **9527[9526]. Application to Commission for Review – No Change**

### **9530. Suspension or Cancellation for Failure to Pay Dues, Fees and Other Charges**

#### **9531. Notice**

(a) Notice – No Change

(b) Service of Notice

Association staff shall serve the notice via personal service, [by] facsimile or overnight [commercial] courier and shall file a copy of the notice with the Office of Hearing Officers.

(c) Effective Date of Notice – No Change

#### **9532. Hearing**

(a) Request for Hearing – No Change

(b) Hearing Procedures

(1) – (3) No Change

(4) Transmission of Documents

Not later than seven days before the hearing, the NASD Treasurer shall serve the member or person associated with a member via overnight [commercial] courier with all documents that were considered in connection with the decision to issue a notice under Rule 9531

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and provide copies of the same to the Hearing Officer.

(5) – (11) No Change

### **9535. Termination of Suspension**

A suspended member or person may file a written request for termination of the suspension on the ground of full compliance with the notice issued under Rule 9531 or, if applicable, the conditions of a decision under Rule 9533, with the Office of Hearing Officers. The Office of Hearing Officers shall respond to the request in writing within five days after receipt of the request. The Office of Hearing Officers shall send the written response via overnight [commercial] courier or facsimile.

### **9540. Failure to Provide Information or Meet the Eligibility and Qualification Standards**

#### **9541. Notice**

##### (a) Notice to Member for Failure to Provide Information

If a member fails to provide any information, report, material, data, or testimony requested or required to be filed pursuant to the NASD By-Laws or the Rules of the Association, or fails to keep its membership application or supporting documents current, the Association staff may provide written notice to such member specifying the nature of the failure and stating that the failure to take corrective action within 20 days after service of the notice constitutes grounds for suspension of membership.

(b) Notice to Person Associated with Member for Failure to Provide Information

If a person associated with a member fails to provide any information, report, material, data, or testimony requested or required to be filed pursuant to the NASD By-Laws or the Rules of the Association, the Association staff may provide written notice to such person specifying the nature of the failure and stating that the failure to take corrective action within 20 days after service of the notice constitutes grounds for suspending the association of the person with the member.

##### (c) Notice to Member for Failure to Meet the Eligibility and Qualification Standards

If a member becomes ineligible for continuance in membership because it does not meet the eligibility and qualification standards set forth in Article III of the By-Laws, the Association staff may provide written notice to such member stating that the failure to become eligible for continuance in membership within 20 days after service of the notice constitutes grounds for cancellation of membership.

##### (d) Service of Notice

The Association staff shall serve the member or person associated with a member with such notice via personal service or overnight courier or by facsimile at the location described in Rule 9134(b). Service by overnight courier shall be accomplished by sending the papers through an overnight courier service that generates a written confirmation of receipt or of attempts at delivery.

##### (e) Effective Date of Notice

A notice issued and served under this Rule shall become effective 20 days after the date of service of the

notice, unless stayed by a request for a hearing pursuant to Rule 9542(a).

### **9542. Hearing**

#### (a) Request for Hearing

Within five days after the date of service of a notice issued under Rule 9541, the member or person served with such notice may file with the Office of Hearing Officers a written request for a hearing. The request shall state with specificity why the member or person believes that the notice should be set aside. The request for the hearing shall stay the effective date of the notice.

#### (b) Hearing Procedures

##### (1) Appointment of Hearing Panel

If a hearing is requested, based upon a notice issued under Rule 9541(a) or (b), the Chief Hearing Officer shall assign a Hearing Officer to preside over the matter, and appoint Panelists pursuant to Rules 9231 and 9232 to the Hearing Panel. As soon as practicable after the assignment, the Chief Hearing Officer shall serve the Parties with notice of the Hearing Panel. Recusals and disqualifications of Hearing Officers and Hearing Panels shall be governed by Rules 9233 and 9234.

##### (2) Appointment of a Hearing Officer

If a hearing is requested, based upon a notice issued under Rule 9541(c), the Chief Hearing Officer shall assign a Hearing Officer to conduct the hearing. As soon as practicable after the assignment, the Chief Hearing Officer shall serve the Parties with notice of the Hearing Officer. Recusals and disqualifications of

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Hearing Officers shall be governed by Rule 9233.

### (3) Parties

The Parties shall be the member or person to whom the notice was issued and the head of the department or office that issued the notice under Rule 9541.

### (4) Time of Hearing

The hearing shall be held within 45 days after the date of service of the notice under Rule 9541. Not later than seven days before the hearing, the Hearing Officer shall serve the Parties with written notice of the date and time of the hearing.

### (5) Transmission of Documents

Not later than seven days before the hearing, the head of the department or office that issued the notice under Rule 9541 shall serve the member or person associated with a member, either personally or via overnight courier, with all documents that were considered in connection with the decision to issue a notice under Rule 9541 and provide copies of the same to the Hearing Officer.

### (6) Counsel

The Parties may be represented by counsel at a hearing conducted under this Rule.

### (7) Evidence

Formal rules of evidence shall not apply to a hearing under this Rule. Not later than four days before the hearing, the Parties shall exchange copies of proposed hearing exhibits and witness lists and provide copies

of the same to the Hearing Officer.

### (8) Witnesses

A person who is subject to the jurisdiction of the Association shall testify under oath or affirmation. The oath or affirmation shall be administered by a court reporter or a notary public.

### (9) Additional Information

At any time during its consideration, the Hearing Officer may direct the Parties to submit additional information. Any additional information submitted shall be provided promptly to all Parties at least one business day before the Hearing Panel renders its decision.

### (10) Transcript

The hearing shall be recorded and a transcript prepared by a court reporter. A Party may purchase a copy of the transcript from the court reporter at prescribed rates. A witness may purchase a copy of the transcript of his or her own testimony from the court reporter at prescribed rates. Proposed corrections to the transcript may be submitted by affidavit to the Hearing Officer within a reasonable time determined by the Hearing Officer. Upon notice to the participants in the hearing, the Hearing Officer may order corrections to the transcript as requested or sua sponte.

### (11) Record

The record shall consist of all documents that were considered in connection with the decision to

issue a notice under Rule 9541, the notice issued under Rule 9541, the request for hearing filed under Rule 9542, the transcript of the hearing, and each document or other item of evidence presented to or considered by the Hearing Panel. The Office of Hearing Officers shall be the custodian of the record.

### (12) Evidence Not Admitted

Evidence that is proffered but not admitted during the hearing shall not be part of the record, but shall be retained by the custodian of the record until the date when the Association's decision becomes final or, if applicable, upon the conclusion of any review by the Commission or the federal courts.

### (13) Failure to Appear at Hearing

If a member or person fails to appear at a hearing for which he has notice, the Hearing Officer may dismiss the request for a hearing as abandoned, and the notice issued under Rule 9541 shall become final. Upon a showing of good cause, the Hearing Officer may withdraw a dismissal entered pursuant to this subparagraph.

## **9543. Decision**

### (a) Failure to Provide Information

The Hearing Panel may impose any fitting sanction, including fines, suspensions, expulsions and bars, based upon the failure to provide any information, report, material, data, or testimony requested or required to be filed pursuant to the NASD By-Laws or the Rules of the Association, or failure to keep a membership application or

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supporting documents current. The Hearing Panel shall prepare a written decision, and if the Hearing Panel determines that a sanction should be imposed, the written decision shall state the grounds for the sanction, and in the case of a suspension, the conditions for terminating the suspension. A Party sanctioned under this Rule will have the right to appeal such a decision to the National Adjudicatory Council, and the decision will be subject to an NASD Board call for review, in accordance with the Rule 9300 Series. If not timely appealed or called for review, the Hearing Panel decision shall constitute final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1).

### (b) Failure to Meet the Eligibility and Qualification Standards

The Hearing Officer may cancel the membership of any member who is ineligible for continuance in membership because it does not meet the eligibility and qualification standards set forth in Article III of the By-Laws. The Hearing Officer shall prepare a written decision, and if the Hearing Officer determines that a cancellation

should be imposed, the written decision shall state the grounds for the cancellation. A member canceled under this Rule will have the right to appeal such a decision to the National Adjudicatory Council, and the decision will be subject to an NASD Board call for review, in accordance with the Rule 9300 Series. If not timely appealed or called for review, the Hearing Officer decision shall constitute final disciplinary action of the Association for purposes of SEC Rule 19d-1(c)(1).

### **9544. Defaults**

Respondents may file motions for reinstatement with the head of the department that issued the original pre-suspension notice under Rules 9541(a) or (b) within six months of the date of the original pre-suspension notice. If such a motion is filed, a Hearing Panel will be convened under Rule 9542, and the Hearing Panel may impose any fitting sanction. Respondents who are suspended pursuant to Rules 9541(a) or (b) and who fail to request hearing to challenge the suspensions within six months of receipt of the pre-suspension notice issued under Rules 9541(a) or (b)

will automatically be barred or expelled.

### **9545. Notice to Membership**

The Association shall provide notice of a suspension, expulsion, cancellation, or bar under this Rule Series and the grounds therefor in the next membership supplement.

### **9546. Copies of Notices and Decisions to Member**

A copy of a notice or decision under the Rule 9540 Series that is served on a person associated with a member shall be served on such member.

### **9547. Other Action Not Foreclosed**

Action by the Association under the Rule 9540 Series shall not foreclose action by the Association under any other Rule.

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