

that a temporary cease and desist order cannot be issued for technical violations of rules; it can be issued only if the violative conduct or the continuation thereof is likely to result in significant dissipation or conversion of assets or other significant harm to investors before completion of the underlying disciplinary proceeding.

A hearing panel must issue a written decision within ten days of receiving the transcript of the hearing, unless otherwise extended by the Hearing Officer with the consent of the Parties upon a showing of good cause. If a hearing panel decides that a temporary cease and desist order should be issued, the order must direct the respondent to cease and desist from violating a specific rule or statutory provisions, and, where applicable, to cease and desist from dissipating or converting assets or causing other harm to investors. The order also must set forth the alleged violation and the significant dissipation or conversion of assets or other significant harm to investors that is likely to result without the issuance of the order, and it must describe in reasonable detail the act or acts the respondent is to take or refrain from taking. A temporary cease and desist order issued to stop unauthorized trading, for example, would order a respondent to cease and desist from violating NASD Rule 2110 by directing the respondent to stop the practice of executing unauthorized trades for customers' accounts. The order would not instruct the respondent to cease and desist conducting business with customers.

2. Publicizing Issuance of a Temporary Cease and Desist Order

If a hearing panel issues a temporary cease and desist order, NASD would publicize the issuance of the order, just as it publicizes the issuance of decisions in disciplinary proceedings that result in significant sanctions. Accordingly, the proposed rule change modifies IM-8310-2 to permit the release of this information. When issuance of a temporary cease and desist order is made public, if applicable, a statement would accompany the public release indicating that the decision could still be appealed to the SEC or that the appeal is pending.

3. Duration of Temporary Cease and Desist Orders

Once a temporary cease and desist order has been issued, it will remain in effect until a decision is issued in the

underlying disciplinary proceeding.¹² In any disciplinary proceeding for which a temporary cease and desist order has been issued, every hearing shall be held and every decision shall be rendered at the earliest possible time.

In addition, if a respondent believes the underlying disciplinary proceeding is not being conducted on an expedited basis, the respondent may seek to have the order modified, set aside, limited or suspended under proposed Rule 9850.¹³

Further, the respondent may seek to challenge a temporary cease and desist order by filing an application for review with the SEC pursuant to Section 19 of the Act.¹⁴ A respondent's application to challenge an order, however, will not stay the effectiveness of the order, unless otherwise ordered by the Commission.¹⁵

4. Enforcement of Cease and Desist Orders

The proposed rule change provides the NASD with the authority to suspend or cancel a respondent's membership or association if it is found, after a proceeding pursuant to the Rule 9510 Series,¹⁶ that a respondent violated a temporary cease and desist order or a permanent cease and desist order. The proposed rule change provides that a proceeding to suspend or cancel a respondent's association or membership for violating an order cannot be initiated unless it is authorized in writing by the President of NASD Regulatory Policy and Oversight or the Executive Vice President for NASD Regulatory Policy and Programs. NASD believes that this provision ensures that decisions that can have a significant impact on a respondent are made only at the highest staff level.

In addition, in any proceeding initiated pursuant to the Rule 9510 Series to sanction a member or associated person for violating a temporary or permanent cease and

desist order, NASD would be required to specifically identify in the notice initiating the proceeding the provision of the temporary or permanent cease and desist order that is alleged to have been violated, and the notice must contain a statement of facts specifying the alleged violation.

5. Two-Year Trial Period for Proposed Rule Change

NASD recognizes that temporary cease and desist orders are new and powerful enforcement tools. Therefore, NASD believes the proposed rule change should be adopted on a trial basis, for a two-year period.¹⁷ At the expiration of the two-year period, NASD will review its experience with temporary cease and desist orders, and, if it believes the proposed rule change should be extended or adopted on a permanent basis, NASD will file a proposed rule change with the Commission seeking an extension or adoption. The proposed rule change will describe the staff's experience with the rule and its basis for seeking extension or adoption.

6. Context in Which Permanent Cease and Desist Orders Will Be Sought

NASD staff does not anticipate seeking permanent cease and desist orders on a routine basis. Factors that NASD staff will consider in determining whether a permanent cease and desist order is appropriate include whether the party's violation was isolated or part of a pattern, whether the violation was flagrant and deliberate or merely technical in nature, and whether the party's business will present opportunities to engage in future violative conduct.¹⁸

II. Summary of Comments

The Commission received five comment letters on the proposed rule change.¹⁹ While all of the commenters applauded the NASD's objective of effective enforcement and fair regulation

¹² The Hearing Panel issuing the decision in the underlying disciplinary proceeding, however, may issue a permanent cease and desist order as part of any sanctions imposed pursuant to the underlying disciplinary proceeding. NASD will not stay the effectiveness of a permanent cease and desist order if the respondent appeals the decision in the underlying disciplinary proceeding.

¹³ See Amendment No. 5.

¹⁴ Section 19 of the Act provides for the appeal of final disciplinary sanctions imposed by self-regulatory organizations ("SROs").

¹⁵ See Amendment No. 5.

¹⁶ The Rule 9510 Series sets forth the procedures for summary and non-summary suspension, cancellation, bar, limitation, or prohibition. Pursuant to the proposed amendment to Rule 9511, the sanctions for a violation of a temporary or permanent cease and desist order are limited to suspension or cancellation of the membership of a member or the registration of a person.

¹⁷ See Amendment No. 4.

¹⁸ See Amendment No. 3. *Cf. In Re KPMG*, Exchange Act Release No. 43862 (Jan. 12, 2001), petition denied, 289 F.3d 109 (D.C. Cir. 2002), where the SEC indicated that in determining whether a cease and desist order is appropriate, it would consider factors that provide some showing of risk of future violation, although such showing need not be as great as that required for the imposition of an injunction. The NASD staff states that nothing in this proposed rule change is intended to impose any standards on NASD staff in exercising its prosecutorial discretion in any particular matter, nor is it intended to require that Hearing Officers find that the standards advocated by the SEC in the *KPMG* litigation described above are met in imposing a permanent cease and desist order. See Amendment No. 5.

¹⁹ See *supra* note 5.