

submitted Amendment No. 2 to the proposed rule change.<sup>4</sup> The proposed rule change, as amended, was published for comment in the **Federal Register** on June 4, 2003.<sup>5</sup> The Commission received a comment on the proposal from the Association of Registration Management ("ARM") on June 25, 2003.<sup>6</sup> The NASD responded to this comment by amending the filing on July 1, 2003.<sup>7</sup> The Commission received a second comment on June 26, 2003<sup>8</sup> and the NASD responded to this comment on July 3, 2003.<sup>9</sup> This order approves the proposed rule change, as amended. In addition, the Commission is publishing notice to solicit comment on and is simultaneously approving, on an accelerated basis, Amendment No. 3 to the proposal.

## II. Summary of Comments and Response to Comments

### A. ARM Comment

As stated above, the Commission received the ARM Comment on the proposed rule change on June 25, 2003, in which ARM made two primary arguments. First, ARM asserted that the information being sought by the introduction of questions 14D(2)(a) and (b) on the Form U-4 is redundant of the information already being sought by existing question 14D on the Form U-4. Moreover, ARM argued that this addition of a new question would "present a monumental task to [the securities] industry" due to the sheer number of Form U-4 amendments that

would be effective on July 14, 2003, instead of June 30, 2003.

<sup>4</sup> See letter from Patrice M. Gliniecki, Vice President and Deputy General Counsel, NASD, to Katherine England, Assistant Director, Division, Commission, dated April 29, 2003 ("Amendment No. 2"). In Amendment No. 2, NASD amended the filing to correct typographical errors on pages 51 of 100 and 68 of 100 of the filing. On page 51 of 100, the NASD added the following language to renumbered question 14D(1)(e): "denied, suspended, or revoked your registration license or." On page 68 of 100, the NASD eliminated the word "or" before "commodities exchange."

<sup>5</sup> See Securities Exchange Act Release No. 47936 (May 28, 2003), 68 FR 33545.

<sup>6</sup> See letter from Mario Di Trapani, President, ARM, to Jonathan G. Katz, Secretary, Commission (June 24, 2003) ("ARM Comment").

<sup>7</sup> See letter from Patrice M. Gliniecki, Vice President and Deputy General Counsel, NASD, to Katherine A. England, Assistant Director, Division, Commission (July 1, 2003) ("Amendment No. 3") (The Commission notes that the NASD inadvertently numbered Amendment No. 3 as Amendment No. 1).

<sup>8</sup> See letter from Dan Jamieson ("Jamieson") to Jonathan Katz, Secretary, Commission (June 26, 2003) ("Jamieson Comment").

<sup>9</sup> See e-mail from Richard E. Pullano, Associate Vice President/Chief Counsel Registration & Disclosure, NASD, to Katherine A. England, Assistant Director, Division, Commission (July 3, 2003) ("NASD Response").

would be required. ARM noted its concern that, upon the introduction of the new question, "every registered person in NASD's WebCRD database (approximately 650,000 individuals) would \* \* \* immediately have an *incomplete* Form U-4 on file." Second, ARM argued that the expanded definition of statutorily disqualified person, contained in the Sarbanes-Oxley Act, extends to non-registered individuals as well as registered individuals. In order to capture non-registered persons (and decrease the administrative burden on member firms), ARM suggested an annual certification procedure in which broker-dealer employees would certify their answers to the proposed questions instead of adding the new questions to the Form U-4.

### B. Amendment No. 3

NASD responded to the ARM comment through Amendment No. 3. In Amendment No. 3, NASD conceded that there is an overlap between the information elicited by current Question 14D and proposed Question 14D(2), but that the literal language of current Question 14D does not specifically require individuals to report final orders of the National Credit Union Administration ("NCUA") or state credit union regulators. Further, NASD does not agree with ARM that it may be implied on the basis of the current Form U-4 definition of "investment-related" that such orders should be reported under current Question 14D. In light of the fact that the Sarbanes-Oxley Act created a new set of statutory disqualifications, NASD, representatives of other self-regulatory organizations, and state regulators (including representatives of the North American Securities Administrators Association ("NASAA")), made a policy decision that, although Question 14D currently requires firms to report most events that may cause an individual to become statutorily disqualified under the Sarbanes-Oxley Act, the forms should be amended to require firms and individuals to report all such information (in response to questions that specifically track the language of the Sarbanes-Oxley Act) in a new question.

NASD disagreed with ARM's suggestion that, as an alternative to including these questions on the forms, NASD should adopt a rule that would require firms to have their employees certify annually their answers to the proposed questions. First, NASD stated that it does not believe that this approach would save time and effort, since it likely would require firms to

establish a methodology for requesting and collecting this information on paper. Second, NASD noted its belief that firms and individuals should be required to report timely (rather than annually) all statutorily disqualifying events on the Forms, including statutorily disqualifying events pursuant to the Sarbanes-Oxley Act.

Also in Amendment No. 3, NASD provided an in depth discussion of how it intends to ease the administrative burden on firms with which the ARM Comment was concerned. The NASD noted that beginning July 14, 2003, it will implement procedures with respect to filing answers to proposed Question 14D(2).<sup>10</sup> NASD noted generally that a change to a disclosure question or the addition of a new disclosure question on Form U-4 requires the prompt filing of an amended Form U-4 only if a registered person is subject to an action or event that requires an affirmative response to the changed or new question or additional disclosure on detailed DRPs relating to the new or changed question. Firms making such amendments to Section 14 (Disclosure Questions) or any DRP also generally are required to complete Section 15D of the Form U-4 (the Individual/Applicant's Amendment Acknowledgment and Consent). If a registered person has not been the subject of an action or event that is elicited by a changed or new disclosure question, he or she need not answer the changed or new disclosure question until an amended Form U-4 filing is otherwise required (e.g., with the filing of a change of address, a request for a new registration category or license, or any new or amended responses to the questions in Section 14 or related DRPs).

Further, the NASD elaborated that, with respect to the proposed new Question 14D(2), firms need to determine immediately whether their registered persons have been subject to an action that requires reporting under the new question. Firms then will be required to amend Forms U-4 to respond to Question 14D(2) promptly (i.e., not later than 30 days from implementation of the new question or August 13, 2003). Registered persons will be required to amend their Form U-4 by August 13, 2003 only when a firm has determined that one of its registered persons must answer "yes" to any part of Question 14D(2). Firms must obtain a completed Form U-4 Section 15D (the Individual/Applicant's Amendment Acknowledgment and Consent) in such

<sup>10</sup> In addition, NASD will publish a Notice to Members explaining these procedures and publish these procedures on the NASD Web Site.