

member must review and, if necessary, update its emergency contact information, including designation of two emergency contact persons, within 17 business days after the end of each calendar quarter to ensure the information's accuracy. The member's Executive Representative must conduct such review and any update. Furthermore, members must have adequate controls and procedures to ensure that only the Executive Representative may perform the review and update.

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

In its filing with the Commission, the NASD included statements concerning the purpose of and basis for the proposed rule change, as amended, and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The NASD has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

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

1. Purpose

The NASD's original proposal and the NYSE's proposal elicited comments from three parties.¹¹ The NASD addressed these comments in Amendment Nos. 1, 2, and 3, which the Commission published for comment in the **Federal Register** on March 10, 2003.¹² The NASD incorporates the interpretations in the Original Notice and **Federal Register** release of March 10, 2003, to the extent that they are consistent with the interpretations contained in this release. The amended proposals of the NASD and NYSE

relating to business continuity planning also elicited comments from three parties.¹³

The purpose of Amendment No. 4 is to clarify that the proposed rule change does not mandate that members stay in business in the event of a significant business disruption. This amendment also would require each member to disclose to its customers how its business continuity plan addresses the possibility of a future significant business disruption. In addition, the amendment would require each member to review and, if necessary, update its emergency contact information on a quarterly basis. Amendment No. 5 clarifies the implementation date of the proposed rules.

Proposed NASD Rule 3510

• Requirement that Plans be Reasonably Designed to Enable the Member to Continue its Business

Proposed NASD Rule 3510(a) would require that members create and maintain business continuity plans. Amendment No. 3 amended the language of the proposed rule to provide that each member's plan be "reasonably designed to enable the member to continue its business in the event of future significant business disruption." As explained in the Original Notice, the NASD intended for proposed NASD Rule 3510 to require that a member not only conduct a planning process to create a written business plan, but also that the resultant plan ensure that member's ability to continue its business in the event of a significant business disruption.

One commenter expressed concern that the language added to proposed NASD Rule 3510(a) would create a new obligation on a member to continue its business after a significant business disruption.¹⁴ This is not the intention of the proposal. The proposal would not deprive a member of its autonomy to choose to cease its operations at any time, provided it does so in a manner consistent with applicable laws and Commission and NASD rules. Nonetheless, to clarify that the rule would not create a new obligation for members to continue their businesses,

NASD is amending the proposed rule. Specifically, the proposed rule text stating that "[s]uch procedures must be reasonably designed to enable the member to continue its business in the event of future significant business disruptions" is amended to read, "[s]uch procedures must be reasonably designed to enable the member to meet its existing obligations to customers. In addition, such procedures must address the member's existing relationships with other broker-dealers and counterparties."

The general principle that firms are not required to remain in business is further recognized in a related amendment that the NASD is proposing to make with respect to the categories that a member's plan must, at a minimum, address. In particular, following discussions with Commission staff and NYSE staff, the NASD is proposing to amend proposed NASD Rule 3510(c) to require a plan to address how a member will assure customers' prompt access to their funds and securities in the event that the member determines it is unable to continue its business.¹⁵ If a member has customers, the member must detail the procedures it would employ to ensure customer access to funds and securities. This new category would help to ensure that if a member were unable to continue its business following a significant business disruption, those customers holding funds or securities through the member would be able to access their funds and/or securities.

• Requirement to Update Business Continuity Plans

Proposed NASD Rule 3510(b) states, "[e]ach member must update its plan in the event of any material change to the member's operations, structure, business or location. Each member must also conduct an annual review of its business continuity plan to determine whether any modifications are necessary in light of changes to the member's operations, structure, business, or location." One commenter suggested that the annual review should be required at the plan component level (either defined by business function or department), rather than the firm level.¹⁶ The NASD continues to believe, however, that each member should annually review the contents of its business continuity plan at the overall firm level. Such a firm-level review would, among other things, help to

¹¹ One commenter submitted a single letter that addressed both proposals. See letter from Melvyn Musson, Edward D. Jones & Co. ("Edward Jones"), to Jonathan G. Katz, Secretary, Commission, dated September 30, 2002. A second commenter submitted two letters that addressed each proposal separately. See letters from Jerry W. Klawitter, Securities Industry Association and Bond Market Association ("SIA/BMA"), to Margaret H. McFarland, Deputy Secretary, Commission, dated September 30, 2002. A third commenter submitted a letter that addressed only the NASD proposal. See letter from Frances M. Stadler, Investment Company Institute, to Jonathan G. Katz, Secretary, Commission, dated September 30, 2002.

¹² See *supra* note 7. The Commission also published for comment Amendment No. 3 to the NYSE's proposal relating to business continuity planning. See *supra* note 10.

¹³ Two commenters responded only to the NASD proposal. See letter from Melvyn Musson, Edward Jones, to Jonathan G. Katz, Secretary, Commission, dated March 28, 2003 ("Edward Jones Letter"); letter from Thomas K. Heard, A.G. Edwards & Sons, Inc., to Jonathan G. Katz, Secretary, Commission, dated March 31, 2003 ("A.G. Edwards Letter"). One commenter, the SIA/BMA, submitted a separate letter in response to each notice. See letters from Jerry W. Klawitter, SIA/BMA, to Jonathan G. Katz, Secretary, Commission, dated March 31, 2003 ("SIA/BMA Letter"), and April 24, 2003.

¹⁴ See SIA/BMA Letter.

¹⁵ The NYSE also is proposing a substantially similar amendment. See Securities Exchange Act Release No. 48502 (September 17, 2003) (Amendment No. 4 to NYSE proposal relating to business continuity planning).

¹⁶ See A.G. Edwards Letter.