

consist of a Regulatory Element and a Firm Element as set forth below.

(a) Regulatory Element

(1) through (6) No change.

(7) *Regulatory Element Contact Person*

Each member shall designate and identify to NASD (by name and e-mail address) an individual or individuals responsible for receiving e-mail notifications provided via the Central Registration Depository regarding when a registered person is approaching the end of his or her Regulatory Element time frame and when a registered person is deemed inactive due to failure to complete the requirements of the Regulatory Element program, and provide prompt notification to NASD regarding any change in such designation(s). Each member must review and, if necessary, update the information regarding its Regulatory Element contact person(s) within 17 business days after the end of each calendar quarter to ensure the information's accuracy.

(b) No change.³

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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 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

NASD Rule 1120 sets forth the CE requirements for registered persons. One of the two CE components is the Regulatory Element, a computer-based education program administered by the NASD to help ensure that registered persons are kept up-to-date on regulatory, compliance, and sales practice matters in the industry. Each registered person is required to

complete the Regulatory Element initially within 120 days after the person's second registration anniversary date and, thereafter, within 120 days after every third registration anniversary date. A registered person who becomes inactive for failing to complete the required Regulatory Element program ("CE inactive") is prohibited from performing, or being compensated for, any activities requiring registration, including supervision. Members are required under NASD Rule 1120 to restrict CE inactive persons from performing the prohibited activities.

To help firms keep track of their registered persons' Regulatory Element status, NASD provides members with e-mail notifications through Web CRD when a person is both 90 days and 30 days away from the end of his or her period to complete the Regulatory Element program before going inactive. CRD also notifies members when a registered person at the firm becomes CE inactive. Currently, receipt of the e-mail notifications is optional, and some firms have elected not to receive the notifications. The proposed rule change would require each member to designate a contact person or persons to receive such CRD Regulatory Element e-mail notifications. The member would be required to provide to the NASD the name and e-mail address of the designated contact person(s) and to promptly notify the NASD of any changes to the information. The NASD intends to collect the contact information through the NASD Contact System⁴ on the NASD Web site.

To ensure the accuracy of the CE contact information, the proposed rule change also would require that each member review and, if necessary, update its CE contact person information within 17 business days after the end of each calendar quarter.⁵

⁴ Effective as of December 8, 2003, the NASD Contact System replaced the Member Firm Contact Questionnaire, the previous system used for members to update and maintain certain required contact information.

⁵ This proposed schedule is consistent with a member's quarterly FOCUS reporting schedule, as well as with the proposed rule change regarding members' business continuity plans. See Securities Exchange Act Release No. 46444 (August 30, 2002), 67 FR 57257 (September 9, 2002) (File No. SR-NASD-2002-108); Securities Exchange Act Release No. 47441 (March 4, 2003), 68 FR 11432 (March 10, 2003) (Notice of Filing of Amendment Nos. 1, 2, and 3 of File No. SR-NASD-2002-108); Securities Exchange Act Release No. 48503 (September 17, 2003), 68 FR 55686 (September 26, 2003) (Notice of Filing of Amendment Nos. 4 and 5 of File No. SR-NASD-2002-108). The Commission notes that these filings are pending at the Commission, and would require members to review and update emergency contact information within 17 business days after the end of each calendar quarter. Similarly, the proposed schedule is consistent with a proposed

The NASD is examining different methods of reminding members of the obligation to quarterly review and update contact person information, including the possibility of a Web page linked to the act of filing the FOCUS report that would prompt members to update such contact person and/or through e-mail reminders to the designated CE contact person.⁶

The NASD believes that the proposed rule change will help firms avoid an NASD Rule 1120(a) violation that would occur if an inactive person were permitted to perform, or receive compensation for, activities that required registration during the period of inactive status. Specifically, the notifications will ensure that firms are positioned to prevent any registered persons from becoming inactive, thus enabling firms and individuals to avoid violations that occur when persons prohibited from doing business due to a CE inactive status nonetheless conduct business or improperly receive compensation.

The NASD also believes the proposed rule change is designed to assist the NASD with its efforts to further automate various aspects of its examination program with a goal of removing a substantial portion of CE compliance inspections from on-site firm examinations. The NASD believes that a more automated approach will result in a more efficient use of the NASD Department of Member Regulation resources and lead to a less intrusive regulatory approach for firms.

2. Statutory Basis

The NASD believes that the proposed rule change is consistent with the provisions of section 15A(b)(6) of the Act,⁷ which requires, among other things, that NASD's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The NASD believes that the proposed rule change is designed to accomplish these ends by helping firms ensure that their registered persons complete the required Regulatory Element training and are prevented from conducting business if they become CE inactive.

rule change filed with the Commission regarding the review and update of a member's Executive Representative designation and contact information. See SR-NASD-2003-184.

⁶ Similarly, NASD would prompt members to review and update, where necessary, their emergency contact and Executive Representative information. See *supra* note 4.

⁷ 15 U.S.C. 78o-3(b)(6).

³ Subparagraph (c) was renumbered to subparagraph (b) to accurately reflect the current text of NASD Rule 1120. Pursuant to a telephone conversation between Grace Yeh, Counsel, NASD, and A. Michael Pierson, Law Clerk, Division of Market Regulation ("Division"), Commission, dated, December 22, 2003.