



Securities Industry Association

120 Broadway, New York, NY 10271-0080, (212) 608-1500, Fax (212) 608-1604
1401 Eye Street, NW, Washington, DC 20005-2225, (202) 296-9410, Fax (202) 296-9775
info@sia.com, <http://www.sia.com>

Via – Federal Express

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Ms. Barbara Z. Sweeney
Office of the Corporate Secretary
NASD
1735 K Street, NW
Washington, D.C. 20006-1500

Mr. Donald Van Weezel
Vice President, Regulatory Affairs
New York Stock Exchange
20 Broad Street, 23rd Floor
New York, NY 10005

Dear Ms. Sweeney and Mr. Van Weezel:

The Securities Industry Association¹ (“SIA”) appreciates the opportunity to respond to the New York Stock Exchange (“NYSE”) and NASD survey letter sent to joint members soliciting information on regulatory inconsistency and the coordinated examination process. Specifically, the survey letter requests that firms identify any inconsistency between SEC, NYSE and NASD rules or interpretations that firms believe cause unnecessary operational inefficiencies.

SIA commends the NASD and NYSE for undertaking this important review and hopes that this joint effort will produce significant change to the existing regulatory rulemaking regime. SIA has long advocated harmonizing self-regulatory organization (“SRO”) rules and examinations. Indeed, SIA did and continues to provide extensive comment to the NASD, both in the form of written submissions and individual dialogue with the staff, in connection with the NASD 1998 “obsolete rule” review, as well the

¹ The Securities Industry Association brings together the shared interests of nearly 700 securities firms to accomplish common goals. SIA member firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of nearly 80 million investors directly and indirectly through corporate, thrift, and pension plans, and generates \$358 billion of revenue. Securities firms employ approximately 760,000 individuals in the United States. (More information about SIA is available on its home page: <http://www.sia.com>.)

more recent “rule modernization” initiative.² In addition, SIA’s membership held several meetings and discussions with the United States General Accounting Office (“GAO”) in preparation of its report entitled *Securities Markets: Competition and Multiple Regulators Heighten Concerns about Self-Regulation* (“GAO Report” or “Report”), during which we identified multiple areas of SRO rule overlap and differences.

As before, we reiterate that both duplicative and conflicting regulation across SROs, as well as government regulators, yields little benefit while depleting valuable administrative and economic resources from all segments of the securities industry. This includes not only the cost of compliance and supervision to broker-dealers, but needless expenditure of valuable staffing and operating resources by regulators to monitor and examine broker-dealer activity on substantially identical or similar subjects.

Clearly, existence of multiple sets of rules governing identical areas is not burdensome *per se*. The difficulty arises, however, when there is a slight variation of language in one rule or a subsequent amendment to, or interpretation of parallel regulation. In such instances, there can be uncertainty, confusion or even discrepancies. More so, particularly within the realm of customer protection rules, inconsistencies result in different levels of investor protection based solely upon their firm’s SRO affiliation.

For these reasons, we strongly support the GAO’s recommendation that the SEC work with the SROs and broker-dealer community to implement a formal process for systemically identifying and harmonizing material regulatory inefficiencies caused by differences in rules or rule implementation among SROs. In fact, SIA made a similar suggestion to the SEC in connection with its special study on Commission operations, efficiency, and resources. There, SIA proposed the SEC require SROs, when making a rule filing, to justify both the need for a particular rule proposal, as well as any inconsistency or non-conformity to existing rules of other SROs. Such a mechanism, we believe, would greatly enhance the quality of SRO rule proposals by promoting more reflective submissions of SRO rules proposals, as well as efficiency of Rule 19b-4 rule reviews.

More fundamentally, we recommend that the NYSE and NASD participate in a joint Regulatory Review Committee to screen rule proposals relating to regulation of broker-dealers in order to identify, and resolve possible inconsistencies, before the proposals are submitted to the SEC pursuant of Rule 19b-4.

Once again, we recommend that the SEC, NASD and NYSE utilize the resources and expertise of SIA and its membership in reviewing and crafting regulation. This collaborative effort, we believe, will foster more constructive, balanced, resource-

² See SIA comment letters to NASD Notice to Members 98-81, dated February 23, 1999 and Notice to Members 01-35, July 31, 2000, both of which are attached.

efficient regulation that ultimately benefits all segments of the industry. SIA would be pleased to assemble a Joint Industry Advisory Group of compliance, operations and legal professionals representing a cross-section of firms to assist your staff in assessing and expanding many of the issues raised herein.

Finally, we note that while we attempted to identify as many rules as possible, this letter is not intended to be all-inclusive. Rather, the comments furnished herein simply highlight some of the areas, and in some instances possible solutions, that are already part of the ongoing regulatory dialogue upon which we hope to build as this process moves forward. We also commend the SROs for being receptive to industry input, and for initiating measures in certain instances with a view toward eliminating inconsistencies.

Specific Comments

1. Institutional Sales Material

NASD Rule 2210 requires supervisory pre-approval of "advertisement" and "sales literature." Under a current NASD rule proposal ("Advertising Rule Proposal"), any material sent or made available only to institutional investors would be excluded from the definition of "advertisement" and "sales literature," and thus from supervisory pre-approval requirements.

NYSE Rule 472(a), by contrast, requires supervisory pre-approval of any "advertisement, market letter, sales literature or other similar type of communication which is generally distributed or made available by a member or member organization to customers or the public." We therefore urge the NYSE to conform its rule to that of the NASD Advertising Rule Proposal.

2. Group E-Mails and Correspondence

The Advertising Rule Proposal also would exclude any material sent or made available only to existing retail customers and/or 25 or fewer potential retail customers from the definition of "advertisement" and "sales literature," and thus from supervisory pre-approval requirements.

NYSE Rule 472(a), by contrast, requires supervisory pre-approval of any "advertisement, market letter, sales literature or other similar type of communication which is generally distributed or made available by a member or member organization to customers or the public." As written, it is unclear to what extent group e-mails and

correspondence, if any, would be subject to Rule 472(a). We therefore urge NYSE to clarify this rule so as to specifically exclude any material, including e-mail and correspondence, sent or made available only to existing retail customers and/or 25 or fewer potential retail customers.

3. Supervisory Review of Hard Copy Incoming Correspondence

In 1998, NASD amended Rule 3010(d) to give its member firms flexibility to develop procedures for the review of electronic and written correspondence, without requiring pre-use or pre-distribution review of any correspondence.

NYSE does not provide for such flexibility. Rather, NYSE Interpretation Handbook 342.16/01 requires pre-distribution review of incoming hard copy correspondence directed to registered representatives (ostensibly to check for customer complaints, payments and securities).

4. Reprints and Externally Prepared Material

Proposed NASD Rule 2210 excludes independently prepared reprints from certain filing and content standards; independently prepared reprints are potentially subject to supervisory pre-approval. "Independently prepared reprints" include, among other things, excerpts of previously published articles, as well as certain customized reports concerning registered investment companies.

NYSE Interpretation Handbook 472/07 provides that reprints and other material that are externally prepared are subject to all of the requirements of Rule 472, unless the Exchange grants a specific waiver. Among the factors to be considered in granting a waiver are whether the material was transmitted in its entirety and not prepared at or commissioned by the member.

5. Short Sale Rule

- a. Netting of ADRs and Ordinary Shares for Purposes of the Short Sale Rule - NASD permits the netting of positions; NYSE does not permit netting. The result: a firm must configure programming for purposes of aggregation units differently for OTC and NYSE-listed ADRs. (Shift in NYSE position may impact ability to treat the securities as separate and distinct for other purposes such as NYSE Rule 92.)
- b. Short Interest Reporting - NASD Rule 3360 requires all customer and firm proprietary accounts to be reported. NASD Rule 120 defines customer as

excluding a broker or dealer. Conversely, NYSE Rule 421 states that all customer and proprietary accounts must be reported. However, for purposes of Rule 421, the NYSE does not define customer or give guidance on whether an affiliate or another broker dealer would be a customer.

- c. After Hours Trading Session - NASD Rule 3350 suspends the Short Sale Rule after normal market hours with the exception of orders traded in the Crossing Sessions. NYSE-listed securities transactions executed after 4 p.m. continue to be subject to Short Sale Rule. pursuant to NYSE Rule 440 (and SEC Rule 10a-1).

We would suggest that, for consistency sake, the NYSE should not apply the short sale rule to after hours trading.

- d. Short Sale and "G" Rules: With creation of the Nasdaq Exchange, these rules will have to be conformed, and we would be pleased to provide input regarding an appropriate conformance standard.

6. Customer Complaints

- a. Definition of Customer Complaints - NYSE Rule 351(d) has been interpreted to include both written and verbal complaints. NASD companion Rule 3070(c) and interpretations, however, cover only "written" complaints, which is entirely consistent with other SRO rules and the federal record retention requirements.
- b. Classifications of Reportable Complaints
NYSE established various categories concerning the types of customer complaints and requires reporting by category. NASD has no equivalent requirements.

7. Gift and Gratuity Rules

NYSE Rule 350(a)(3) generally prohibits members or their employees from giving gifts in excess of \$100 to individuals employed by certain financial institution, including other broker-dealers, absent prior consent of the recipient's employer.

NASD Rule 3060 similarly prohibits gifts in excess of \$100 per person, per year "where such payment or gratuity is in relation to the business of the employer." Despite the fact that the NASD rule focuses on the giving of the gift in relation to a person's employment, NASD does not allow for exceptions to the \$100 threshold on the basis of

employer consent.³ We therefore urge the NASD to conform its rule to that of the NYSE so as to permit gifts in excess \$100 limitation upon the employer's prior approval.

8. Transactions by Employees Associated with Other Broker-Dealers

NYSE Rule 407 requires written consent by the employer of the individual seeking to open the account prior to opening such account. Duplicate confirms and statements must be provided to the employee.

NASD Rule 3050 requires notification to the employer of intention to open the account, duplicate confirms and statements must be furnished by or written request. In addition, 3050 imposes an obligation on the executing broker to ensure that there are no transactions that are contrary to the interests of the employer.

9. Representative Reporting/Disclosure Requirements

NYSE Rule 351 and NASD Rule 3070, generally require disclosure of all customer settlements or arbitration awards exceeding \$15,000.

Uniform Registration and Termination Forms U-4 and U-5 respectively, broadly require disclosure of customer settlements or arbitration awards relating only to sales practice allegations of \$10,000 or more. In addition, the U-4 and U-5 requires disclosure of sales practice complaints alleging damages of \$5,000 or more.

We recommend that the reporting requirements be conformed regardless of whether they relate to events occurring during the course of employment or reportable in conjunction with inception or termination of employment.

10. Representative Training Requirements

NYSE Rule 345 requires a four-month waiting period for all representatives prior to the Series 7 becoming effective.⁴

NASD has no equivalent rule.

³ See NASD Interpretive Letter dated June 10, 1999 noting inconsistency with NYSE Rule 351.

⁴ (Supplemental material 245.15(2))

We recommend that the NYSE waiting period be eliminated where the registrant has other meaningful financial services or similar experience.

11. Qualifications of Registered Persons

- a. NYSE requires two months of employment before its member firm candidates can sit for the Series 7 and an additional two months before approving the candidates to act as a General Securities Representative. The NASD permits its member firm candidates to sit for the Series 7 as soon as scheduling permits and will approve them to act as a General Securities Representative immediately upon successful completion of the exam.
- b. NYSE interprets its rule to require the registered person be “employed by” the member firm or subsidiary of the member firm. NASD only requires that the candidate be an “associated person” of the member firm.

12. Supervisory Requirements

NYSE Rule 345 and interpretations there under, requires prospective supervisor to hold a Series 7 for a period of three years prior to assuming supervisory responsibility over registered representatives.

NASD has no equivalent rule.

Similar to our comments regarding item #10, we recommend that this waiting period also be eliminated where the individual has other meaningful supervisory experience.

13. Supervisory Licenses

NYSE Rule 345 and interpretations thereunder require branch office managers, or anyone overseeing sales personnel to obtain a Series 9/10 license, and does not recognize the NASD Series 24 supervisory license in any respect.

NASD recognizes the Series 9/10 as a limited supervisory license as it relates to sales executives and also requires a Series 24 for all other facets of supervision, such as the review and approval of marketing material.

While we understand that recent rule proposals will provide for a greater degree of reciprocity, we reiterate our recommendation for adoption of a single “super” principal exam that will attain true reciprocity between the two examination requirements.

14. Confirmation Disclosure

NYSE Rule 409(f) requires confirmations to show “name” of the market where the transaction was executed. There is no equivalent NASD or SEC rule. The NYSE requirement is burdensome because single orders are often executed in more than one marketplace, and it is also unnecessary since SEC Rule 11Ac1-6 requires disclosure of this information to customers upon request⁵

NASD has no equivalent rule.

15. Branch Offices

- a. Opening of Branch Office - NYSE requires new branch offices be approved by the Exchange whereas NASD only has a notification requirement which can be satisfied via the Form BD amendment.
- b. Definition of Branch Office – NASD Rule 3010(g)(2) essentially defines a branch office as any location advertised as a business location, or any location a member firm otherwise holds out as a place the public may conduct securities business. NYSE Interpretation to Rule 342 defines branch office as an office with three or more registered representatives. We therefore recommend that the definition of branch office, small office, residence as branch and Office of Supervisory Jurisdiction should be conformed, and we understand NAASA, the NYSE and NASD are working toward a common definition.
- c. Branch Office Inspections - NYSE Interpretation 342(a)(b)/03 requires member organizations to conduct an annual inspection of all branch office locations, unless demonstrated to the satisfaction of the exchange that due to proximity, special reporting or supervisory arrangements, certain offices do not warrant annual inspections.

⁵ While our letter is focused on inconsistencies between NYSE and NASD rules, this item illustrates that there are also inconsistencies between SRO and SEC rules which SIA contemplates addressing in future communications

NASD Rule Requires that an “Office of Supervisory Jurisdiction” be inspected each year, but allows members to determine an appropriate frequency of inspection for regular branch offices based on its business.

16. Space Sharing

NYSE Rule 343(a) requires NYSE approval for a member firm to occupy space with any other broker-dealer or person who conducts securities business with the public.

NASD has no equivalent rule

17. Transfer of Accounts Between Two Broker-Dealers of the Same Clearing Firm

The NYSE has provided verbal advice that it is permissible to use negative consent letters to transfer accounts.

NASD Interpretative letter (Merit Capital letter), dated October 10, 2000, generally prohibits the use of negative consent letters to transfer accounts.

18. Trade Review and Investigation

NYSE Rule 342.21 requires members to have procedures in place to identify trades in NYSE-listed securities that may violate the Securities Exchange Act of 1934. Member firms are also required to make quarterly certifications in this regard.

NASD has no equivalent rule.

19. General Securities License (Series 7) for Correspondent Sales Personnel

NYSE has provided verbal advice that individuals solely engaged in marketing correspondent clearing services to introducing broker-dealers are not required to obtain the Series 7. By contrast, presented with the exact same fact pattern, the NASD advised its members that such individuals must obtain the Series 7.

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CONCLUSION

We thank you again for the opportunity to provide input on this important initiative and hope this letter is helpful. We look forward to working with the staff and continuing the regulatory dialogue as this joint effort moves forward. If we can provide any further information or clarification of points made in this letter, please contact Amal Aly, SIA Vice President and Associate General Counsel, at (212) 618-0568 or Michael Udoff, Vice President and Associate General Counsel at (212) 618-0509.

Sincerely,

Michael H. Stone
President
SIA Compliance & Legal
Division

Christopher Franke
Chairman
SIA Self-Regulation & Supervisory
Practices Committee

cc: Mary L. Schapiro - NASD
Eric Moss - NASD
Edward Kwalwasser - NYSE
Salvatore Pallante - NYSE
Annette Nazareth - SEC
Richard Hillman - GAO
Cecile Trop - GAO