



## Securities Industry Association

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February 7, 1997

Joan Conley  
Office of the Corporate Secretary  
NASD Regulation, Inc.  
1735 K Street, NW  
Washington, DC 20006-1500

### **Re: Notice to Members 96-82 Proposed Rules Governing Supervision, Review and Record Retention of Correspondence (December 1996)**

Dear Ms. Conley:

The Technology Regulatory Subcommittee, Federal Regulation Committee, Self-Regulation and Supervisory Practices Committee, and Compliance and Legal Division of the Securities Industry Association ("**SIA**")<sup>1</sup> appreciate the opportunity to provide comments to the National Association of Securities Dealers, Inc. ("**NASD**") regarding proposed amendments to Conduct Rules 3010 (Supervision) and 3110 (Books and Records) (collectively, the "**Proposed Rule Change**").

For the reasons set forth below, SIA strongly supports the Proposed Rule Change and hopes that such amendments will be adopted by the NASD Regulation, Inc. ("**NASDR**") Board of Directors and promptly submitted for approval to the Securities and Exchange Commission (the "**Commission**" or "**SEC**").

We applaud the NASD for its prompt and practical action regarding supervision of customer correspondence. The Commission previously addressed the use of electronic media by broker-dealers, investment advisers and transfer agents in its May 9, 1996 interpretive release.<sup>2</sup> In the release, the SEC strongly encouraged self-regulatory organizations to continue to work with broker-dealers to adapt their supervisory review requirements governing communication with customers to accommodate the use of electronic communication.<sup>3</sup> The New York Stock Exchange ("**NYSE**") was the first self-regulatory organization to respond. On September 12, 1996, it submitted to the SEC for approval proposed amendments to its rules regarding communications with the public, supervision and books and records (the "**NYSE Proposal**").

In a comment letter to the Commission, dated December 9, 1996, SIA voiced strong support for the NYSE Proposal. The NYSE Proposal would give each firm flexibility to develop procedures for review of correspondence tailored to the nature and size of its business and customers.

The Proposed Rule Change would align the NASD's rules on supervision and retention of customer communications with the NYSE Proposal. Such a uniform and consistent regulatory

approach is extremely important to the securities industry. We believe that the Proposed Rule Change not only is directly responsive to the SEC's request for SROs to adapt supervisory rules to accommodate the use of electronic communication, but also is sensible, practical and prudent. A less flexible position would be inconsistent with the NYSE Proposal and likely would result in most firms prohibiting their associated persons from communicating electronically with customers.<sup>4</sup>

A flexible regulatory approach on customer communications offers important benefits to brokerage firm customers, investors and securities markets. In addition to permitting firms to service clients more efficiently and conveniently, such a flexible approach gives customers and investors greater access to information. Capital markets should be more efficient as the flow of information is enhanced and made more equitable. The public may also benefit from the increased attention to firm policies and procedures on supervising communications with the public that is likely to result.

SIA appreciates the fact that the NASD has been actively reviewing its rules and regulatory positions in light of technological advances. The NASD's interpretive guidance rendered over the past year or so has been helpful to the securities industry. Firms are wrestling to apply rules that often were adopted at a time when current uses of communication technology simply were not contemplated, often in the face of increasing customer demand and competitive pressures, and are trying to do so in a responsible manner. The Proposed Rule Change is another positive and helpful step in this process.

We note that the NASD refers to the SEC's proposed amendments to its broker-dealer books and records rules.<sup>5</sup> SIA is concerned that, in at least one respect, the SEC's proposed amendments, if adopted, would conflict both with the Proposed Rule Change and the SEC's call for supervisory rules that accommodate electronic communication. In particular, Rule 17a-4, as proposed for amendment, would require broker-dealers to preserve books and records indicating that all out-going communications have been approved by a principal of the member.<sup>6</sup> The communication approval requirement in the Proposed Rule Change, which does not require review of all communications with the public, is more consistent with the SEC's earlier call for accommodation of new forms of technology. This aspect of the books and records proposal is a step in the wrong direction.<sup>7</sup>

Again, we praise the NASD for its prompt action and for proposing a regulatory approach that is uniform and consistent with the standards proposed by the NYSE. We hope NASDR will approve the Proposed Rule Change and promptly submit it to the SEC for approval.

If you have any questions regarding our letter or would like any further information, please do not hesitate to contact Mark A. Egert, SIA Vice President and Associate General Counsel, at (212) 618-0508.

Very truly yours,

Kenneth S. Spirer, Chairman  
Technology Regulatory Subcommittee  
of Ad Hoc Technology Issues Committee

C. Evan Stewart, Chair  
Federal Regulation Committee

R. Gerald Baker, Chairman  
Self-Regulation and Supervisory Practices Committee

Robert C. Errico, President  
Compliance and Legal Division

**cc:** R. Clark Hooper, NASDR Senior Vice President, Office of Disclosure and Investor Protection  
Mary N. Revell, NASDR Assistant General Counsel, Office of General Counsel

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## Footnotes

1 The Securities Industry Association brings together the shared interests of more than 760 securities firms throughout North America to accomplish common goals. SIA members -- including investment banks, broker-dealers, specialists, and mutual fund companies -- are active in all markets and in all phases of corporate and public finance. In the U.S., SIA members collectively account for approximately 90 percent, or \$100 billion, of securities firms' revenues and employ about 350,000 individuals. They manage the accounts of more than 50-million investors directly and tens of millions of investors indirectly through corporate, thrift and pension plans.

2 See Securities Act Release No. 7288 (May 9, 1996), published in 61 *Federal Register* 24644 (May 15, 1996).

3 *Id.* at note 5, 61 *Federal Register* at 24645 ("The Commission believes . . . that SROs' rules concerning the supervisory requirement for electronic communication should be based on the content and audience of the message, and not merely the electronic form of the communication. . . . SROs should consider whether electronic mail communications, that, as a practical matter replace or substitute for telephone conversations, in many cases, would not require advance authorization or prior supervisory review."). Prior to the SEC release, SIA advocated a flexible regulatory approach regarding email supervision in a letter, dated January 25, 1996, from Stuart J. Kaswell, SIA General Counsel, to Commissioner Steven Wallman, and in meetings with SEC staff.

4 The Proposed Rule Change also is consistent with the Commission's move away from dictating substantive regulatory standards for specific problems and toward an approach based on broad regulatory goals. This enlightened approach gives regulators and firms the flexibility to allow regulations and compliance procedures to evolve with changes in markets, technology and business.

5 See NASD Notice to Members 96-82 at footnote 8 (referring to Exchange Act Release 37850 (Oct. 22, 1996), published in 61 *Federal Register* 55593 (Oct. 28, 1996)).

6 See proposed Rule 17a-4(b)(4), *id.* 61 *Federal Register* at 55600-55601.

7 SIA commented separately (and more extensively) on the books and records release. See

letter, dated January 13, 1997, to SEC from Federal Regulation and Self-Regulation and Supervisory Practices Committees and Compliance and Legal Division.