

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-51860; File No. SR-NASD-2005-061]

### Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Extend for an Additional Two-Year Period NASD's Authority Under the Cease and Desist Pilot Program

June 16, 2005.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on May 11, 2005, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the NASD. NASD has filed the proposal as a "non-controversial" rule change pursuant to Section 19(b)(3)(A) of the Act,<sup>3</sup> and Rule 19b-4(f)(6) thereunder,<sup>4</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

NASD is proposing a rule change to extend for an additional two-year period, to June 23, 2007, NASD's authority under the cease and desist pilot program. At this time, NASD is not proposing any substantive changes to the rules covered by the pilot program. NASD's proposed changes would only extend the pilot's expiration date to June 23, 2007, and make technical changes to certain cross-references in rules covered by the pilot program. Below is the text of the revised rule change. Proposed new language is in *italics*; proposed deletions are in *brackets*.<sup>5</sup>

\* \* \* \* \*

9556. Failure to Comply with Temporary and Permanent Cease and Desist Orders

(Rule 9556, and amendments adopted by SR-NASD-98-80 to Rule 8310, IM-8310-2(d)(1), 9120(x), 9241(c), 9290, 9311(b), 9312(b), 9360 and the Rule 9800 Series, shall expire on June 23, [2005] *2007*, unless extended or permanently adopted by the Association pursuant to SEC approval at or before such date.)

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9800. Temporary Cease and Desist Orders

(The entire Rule 9800 Series, and related amendments adopted by SR-NASD-98-80 to Rule 8310, IM-8310-2(d)(1), 9120(x), 9241(c), 9290, 9311(b), 9312(b), *and 9360, and by SR-NASD-2003-110 to Rule 9556*, shall expire on June 23, [2005] *2007*, unless extended or permanently adopted by the Association pursuant to SEC approval at or before such date.)

\* \* \* \* \*

9860. Violation of Temporary Cease and Desist Orders

A Respondent who violates a temporary cease and desist order imposed under this Rule Series may have its association or membership suspended or canceled under [the] Rule 9556 [9510 Series]. The President of NASD Regulatory Policy and Oversight or the Executive Vice President for NASD Regulatory Policy and Programs must authorize the initiation of any such proceeding in writing.

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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, 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. 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

In May 2003, the Commission approved, on a two-year pilot basis, a rule change that gave NASD authority to issue temporary cease and desist orders

("TCDOs") and made explicit NASD's ability to impose permanent cease and desist orders as a remedy in disciplinary cases.<sup>6</sup> The pilot program also gave NASD authority to enforce cease and desist orders. The pilot program expires on June 23, 2005. NASD proposes to extend the pilot program for an additional two-year period, to June 23, 2007. Such an extension would enable NASD to continue to issue and enforce temporary and permanent cease and desist orders. NASD's authority to issue TCDOs would expire after the additional two-year period, unless the pilot program is further extended or adopted on a permanent basis with Commission approval.

NASD currently seeks only to extend the pilot program period and to make technical changes to certain cross-references in rules covered by the pilot program. NASD is not proposing any substantive changes to the rules covered by the pilot program at this time. Since the pilot program was first approved in 2003, NASD has issued only one TCDO and one permanent cease and desist order (in the same case, which is described below). Consequently, NASD believes that additional time is needed to make a meaningful determination about whether certain specific provisions eventually should be modified and, if so, to what extent.

In the one case initiated under the pilot program, NASD's Department of Enforcement ("Enforcement") alleged that the member in question was engaged in widespread fraud that included, among other things, making material misrepresentations and omissions in connection with the private offering of its own stock, effecting unauthorized transactions, and using customer funds improperly. Enforcement showed that not only was the member attempting to continue the fraudulent offering, it also was funneling money and assets to a non-NASD member affiliate. Enforcement alleged, and a hearing panel found, that a TCDO was necessary because the member's continuation of the misconduct was likely to result in further dissipation or conversion of assets and other significant harm to investors before the completion of the underlying disciplinary proceeding. After the hearing panel issued a permanent cease and desist order following a full disciplinary hearing, the parties settled the case, resulting in the expulsion of the member, the bar of its owner, and the imposition of almost \$12 million in fines and restitution.

<sup>6</sup> See Securities Exchange Act Release No. 47925 (May 23, 2003), 68 FR 33548 (June 4, 2003).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).

<sup>5</sup> NASD represents that the rule language contained in parentheses in NASD Rules 9556 and 9800 is, and will continue to be, italicized in NASD's manual. However, the existing rule language in the parentheses that will not be modified by NASD's proposed rule change is not italicized for purposes of this **Federal Register** publication so that it will not appear as proposed new text.

The proposed extension of the pilot program for an additional two years would provide NASD with a mechanism to continue to take appropriate remedial action against a member or an associated person who has engaged (or is engaging) in violative conduct that could cause continuing harm to the investing public if not addressed expeditiously. At the same time, the pilot program continues to contain numerous procedural checks and safeguards to ensure that cease and desist proceedings are used prudently, sparingly and fairly. In addition, the extension of the pilot program would allow NASD to analyze more thoroughly the pilot program's overall effectiveness. Accordingly, NASD believes it is appropriate to extend the pilot period regarding cease and desist orders for another two years.

The proposed rule change is effective upon filing, would be operative on June 23, 2005, and would expire on June 23, 2007, unless extended or permanently adopted by NASD pursuant to Commission approval at or before such date.

## 2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>7</sup> which requires, among other things, that NASD's rules 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. NASD also believes that the proposed rule change is consistent with the provisions of Section 15A(b)(7) of the Act,<sup>8</sup> which provides that NASD members, or persons associated with its members, are appropriately disciplined for violations of any provisions of the Act or NASD's rules. NASD believes that the extension of the pilot program is consistent with NASD's obligations under the Act because cease and desist orders are designed to stop violative conduct that is likely to cause dissipation or conversion of assets or other significant harm to investors.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

NASD does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants or Others*

NASD has neither solicited nor received comments on the proposed rule change.

### **III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Because the foregoing rule change: (1) Does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) does not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>9</sup> and Rule 19b-4(f)(6) thereunder.<sup>10</sup>

In accordance with Rule 19b-4,<sup>11</sup> NASD submitted written notice of its intent to file the proposed rule change extending the pilot, along with a brief description and text of the proposal, at least five business days prior to the date of filing. NASD proposes to make the proposed rule change operative on June 23, 2005. The rule change would expire on June 23, 2007, unless extended or permanently adopted by NASD pursuant to Commission approval at or before such date.

At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

#### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASD-2005-061 on the subject line.

<sup>9</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>10</sup> 17 CFR 240.19b-4(f)(6).

<sup>11</sup> 17 CFR 240.19b-4.

### *Paper Comments*

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-9303.

All submissions should refer to File Number SR-NASD-2005-061. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of the filing also will be available for inspection and copying at the principal offices of the NASD. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASD-2005-061 and should be submitted on or before July 14, 2005.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>12</sup>

**Margaret H. McFarland,**  
*Deputy Secretary.*

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## **SECURITIES AND EXCHANGE COMMISSION**

**[Release No. 34-51859; File No. SR-NASD-2005-068]**

### **Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing of Proposed Rule Change Regarding a New Order Type for the Pre-Market Trading Session**

June 16, 2005.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the

<sup>12</sup> 17 CFR 200.30-3(a)(12).

<sup>7</sup> 15 U.S.C. 78o-3(b)(6).

<sup>8</sup> 15 U.S.C. 78o-3(b)(7).