

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

The proposed rule change would: (i) change references to "paragraphs (b)(2) and (c)(2)" of NASD Rules 3030 and 3031 to "paragraphs (c)(2) and (d)(2)" in NASD IM-3130(a), (c), (d), and (e); and (ii) change references to "the Association" to "NASD" in NASD IM-3130, thereby conforming the rule language in NASD IM-3130 to the rule language in Rules 3130 and 3131, as recently amended.⁵

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of section 15A of the Act,⁶ in general, and with section 15A(b)(6) of the Act,⁷ in particular, 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 believes that conforming the references in NASD IM-3130 to renumbered paragraphs in recently amended NASD Rules 3130 and 3131 and changing references to "the Association" to "NASD" would be consistent with the protection of investors and the public interest.

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

NASD does not believe that the proposed rule change would result in any burden on competition that is 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

Written comments were neither solicited nor received.

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

Because the foregoing proposed rule change does not:

- (i) significantly affect the protection of investors or the public interest;
- (ii) impose any significant burden on competition; and
- (iii) 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, it has become effective pursuant to section 19(b)(3)(A) of the Act⁸ and Rule 19b-4(f)(6) thereunder.⁹ At any time within 60 days of the filing of the 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.

NASD has requested that the Commission waive the 30-day operative delay. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest. The proposed rule change corrects references to recently amended rules, which should preserve the accuracy of NASD's rules. For these reasons, the Commission designates the proposal to be effective and operative upon filing with the Commission.¹⁰

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. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609.

⁸ 15 U.S.C. 78s(b)(3)(A).

⁹ 17 CFR 240.19b-4(f)(6). The Commission notes that NASD provided written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change at least five business days prior to the date of filing of the proposed rule change.

¹⁰ For purposes only of accelerating the operative date of the proposed rule change the Commission considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

Comments may also be submitted electronically at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File No. SR-NASD-2003-177. This file number should be included on the subject line if e-mail is used. To help the Commission process and review comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. 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 such filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to File No. SR-NASD-2003-177 and should be submitted by January 14, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹¹

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-48932; File No. SR-NASD-2003-186]

Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to the Administration of Qualification Examinations on Security Futures

December 16, 2003.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder,² notice is hereby given that on December 11, 2003, the National Association of Securities Dealers, Inc. ("NASD") submitted to 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. The NASD has filed the proposed rule

⁵ See Securities Exchange Act Release No. 48438 (September 4, 2003), 68 FR 53766 (September 12, 2003) (SR-NASD-2003-74).

⁶ 15 U.S.C. 78o-3.

⁷ 15 U.S.C. 78o-3(b)(6).

¹¹ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4

change pursuant to Rule 19b-4(f)(6) under the Act.³ 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 Proposed Rule Change

In this filing, the NASD discusses the implementation of new and revised qualification examinations to address trading in security futures.

The NASD does not propose to amend any of its existing rule text.

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

The commodity Futures Modernization Act of 2000 ("CFMA")⁴ lifted the ban on the trading of security futures (*i.e.* futures on single stocks and on narrow-based stock indexes). The NASD states that, at the time the CFMA was enacted, expectations for security futures were very high, and two separate markets were developed to trade these new products. To meet the challenge of ensuring that individuals engaging in a security futures business are properly qualified, the NASD took the unique step of mandating that firms include training in security futures as part of their firm-element continuing education program. Furthermore, to assist firms in meeting this responsibility, the NASD and the National Futures Association ("NFA") contracted with the Institute for Financial Markets to develop an internet-based training program. NASD and NFA have made this program available to firms and registered representative for free. Since its inception in October 2002, over 12,000 individuals have completed the Internet

training, which takes approximately two to three hours to complete.

At the time trading in security futures commenced, NASD also indicated that it planned to both modify and create qualification examinations to address trading in security futures. Specifically, NASD intended to modify the Series 4 examination (Registered Options and Security Futures Principal (replacing Registered Options Principal)), Series 9/10 examination (Limited Principal General Securities Sales Supervisor), and Series 42 examination (Limited Representative Options and Security Futures (replacing Limited Representative Options)). In addition, NASD intended to create a new Series 43 examination for general securities representatives (those persons who have successfully completed the Series 7 exam) seeking to engage in a security futures business.⁵ The Series 43 is targeted at new entrants into the securities industry. Existing registrants (*i.e.*, those registered before the Series 43 examination is effective) are required to complete a firm-element continuing education program prior to engaging in a security futures business. Once the Series 43 was developed, NASD intended to permit existing registrants the option of completing the firm-element continuing education program in lieu of the Series 43 examination until December 31, 2006.

In the approximately one year since security futures began trading, NASD has devoted substantial resources to creating the Series 43 examination. Industry and SRO representatives⁶ have met for 11 days and have devoted collectively over 1800 hours in meeting time developing a content outline and a question bank for the Series 43.⁷ In addition, NASD has incurred over \$45,000 in expenses to develop these materials. The Series 43 examination development is now complete. Revised study outlines for the Series, 4, 9/10 and 42 also have been developed. Questions for those examinations will be borrowed from the Series 43 question bank and developed by committees charged with maintaining and reviewing the question banks for those examinations.

Despite these efforts, current data on trading volume has shown that there is very limited trading activity in security

futures. According to data from the Options Clearing Corporation, the average trading volume for 2003 in security futures is around 10,000 contracts per day across the two exchanges. In addition, NASD's market regulation surveillance confirms that most of this volume is proprietary trading among market-maker firms. NFA representatives have informed the NASD that security futures products represented 0.0028% of all futures contracts traded so far in 2003. While similar statistics are not calculated for the securities industry, the figures would be substantially lower given the size of the securities markets.

Moreover, interest among registered representatives to engage in a security futures business has waned. Since July 2003, an average of fewer than 50 registered persons per month in the securities industry have completed the Internet-based continuing education.

In view of the foregoing, the NASD does not believe it is appropriate or necessary to institute the Series 43 exam or amend other existing qualification examinations at the present time. The NASD believes the current system of a firm-element continuing education requirement continues to work well. The NASD states that the feedback it has received on the Internet-training program has been very positive. In addition, the NASD states that it has not received any evidence of customer complaints in these products. Moreover, the NASD is hesitant to amend existing examinations to address security futures because the net result will be to deemphasize other more pertinent subject areas, as the NASD does not intend to expand the number of questions on the Series 4, 9/10, and 42 exams.⁸ Finally, the introduction of a separate, stand-alone qualification examination for security futures seems excessive in view of the level of trading in these products. The NASD also anticipates that very few representatives would elect to take the Series 43 exam.

The NASD notes that its colleagues at NFA have made similar conclusions about the need to revise the Series 3 to reflect trading of security futures. Both NASD and NFA believe that the qualification requirements between the securities and futures industry should generally be comparable, and, as regulators, the NASD has sought to avoid favoring one industry group over another, or actions leading to regulatory arbitrage.

⁵ A new Series 43 examination was necessary, in part, because the New York Stock Exchange did not intend to incorporate questions on security futures on the Series 7 examination.

⁶ SRO representatives from the NASD, NFA, CBOE, AMEX, OneChicago, and NQLX helped develop the content outline and question bank.

⁷ These totals do not include travel time, time spent preparing for meetings (including developing and reprinting questions), and NASD staff time administering the Series 43 program.

⁸ The problem is equally acute on the futures industry side, where the proposed revised Series 3 examination will have approximately 17% of its questions addressing security futures.

³ 17 CFR 240.19b-4.

⁴ P.L. 106-554, 114 Stat. 2763 (December 21, 2000).

While the NASD does not plan to implement the new or revised qualification examinations today, it intends to monitor activity in security futures very closely. The NASD also intends to continue coordinating with NFA. The NASD intends to make periodic assessments of the activity in security futures to determine the appropriate time to implement the examinations. The NASD does not believe that there is any single factor that should be determinative of whether security futures examinations should be implemented. Rather, the NASD intends to review the following:

- Volume in security futures contracts
- Analysis of who is trading security futures
- Number of registered representatives completing continuing education
- Number of accounts authorized to trade security futures
- Nature of security futures customers
- Evidence, if any, of customer complaints
- Evidence, if any, of regulatory concerns arising from the NASD's surveillance and examination programs.

Once the NASD determines that new/ revised qualifications are appropriate, or the SEC requests that the NASD implement the examinations, the NASD represents that it will be able to have them effective in less than four months. The NASD states that, as its efforts to date indicate, it remains fully committed to providing the necessary resources to ensure that representatives engaging in a security futures business are properly trained and qualified. The NASD intends to closely monitor activity in security futures to determine when, and if, it becomes an appropriate date to implement revised qualification examinations.

NASD believes that for the reasons stated above it is appropriate to defer implementation of revised and new qualification examinations concerning security futures.

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of section 15A(b)(6) of the Act,⁹ 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.

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

NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

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

Written comments were neither solicited nor received.

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

The foregoing rule change has been filed by the NASD as "non-controversial" pursuant to section 19(b)(3)(A) of the Act¹⁰ and subparagraph (f)(6) of Rule 19b-4 thereunder.¹¹ 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 thirty 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, it has become effective pursuant to section 19(b)(3)(A) of the Act¹² and Rule 19b-4 thereunder.¹³

The Commission hereby waives the thirty-day operative waiting period. The Commission believes that it is consistent with the protection of investors and the public interest to waive the thirty-day operative waiting period because the proposed rule change explains the NASD's reasons for delaying the implementation of the new qualification exams for security futures.¹⁴ The Commission notes that the NASD members that trade security futures are required to provide firm-element training for individuals engaged in security futures business.

NASD has requested that the Commission waive the five-day pre-filing requirement in Rule 19b-4(f)(6)(iii).¹⁵ The Commission hereby waives that requirement.

At any time within sixty 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. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 fifth Street, NW., Washington, DC 20549-0609. Comments may also be submitted electronically at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File No. SR-NASD-2003-186. 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, comments should be sent in hardcopy or by e-mail but not by both methods. 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 such filing also will be available for inspection and copying at the principal office of the NASD. All submissions should refer to File No. SR-NASD-2003-186 and should be submitted by January 14, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁶

Margaret H. McFarland,
Deputy Secretary.

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¹⁰ 15 U.S.C. 78s(b)(3)(A).

¹¹ 17 CFR 240.19b-4(f)(6).

¹² 15 U.S.C. 78s(b)(3)(A).

¹³ 17 CFR 240.19b-4.

¹⁴ For purposes of accelerating the operative date of the proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

¹⁵ 17 CFR 240.19b-4(f)(6)(iii).

¹⁶ 17 CFR 200.30-3(a)(12).

⁹ 15 U.S.C. 78o-3(b)(6).