

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-55819; File No. SR-NASD-2007-033)

May 25, 2007

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto Relating to Extension of NASD's Authority Under the Cease and Desist Pilot Program

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 May 11, 2007, 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 substantially prepared by NASD. NASD has filed the proposal as a "non-controversial" rule change pursuant to Section 19(b)(3)(A) of the Act³ and Rule 19b-4(f)(6) thereunder,⁴ which renders the proposal effective upon filing with the Commission. On May 24, 2007, NASD filed Amendment No. 1 to the proposed rule change. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

NASD is proposing to amend NASD Rules 9556, 9800, 9810, and 9860, to extend for an additional two-year period, to June 23, 2009, 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. The only changes regard extending the pilot's expiration date to June 23,

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6).

2009, and technical changes to the titles of the NASD executives who can authorize the initiation of cease and desist proceedings and certain cross-references in rules covered by the pilot program.

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in [brackets].

* * * * *

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-8310-3(c)(1) (formerly IM-8310-2(d)(1), renumbered by SR-NASD-2003-168), 9120(x), 9241(c), 9290, 9311(b), 9312(b), 9360 and the Rule 9800 Series, shall expire on June 23, [2007]2009, unless extended or permanently adopted by the Association pursuant to SEC approval at or before such date.)

(a) Notice of Suspension, Cancellation or Bar

If a member, person associated with a member or person subject to NASD's jurisdiction fails to comply with a temporary or permanent cease and desist order issued under the Rule 9200, 9300 or 9800 Series, NASD staff—after receiving written authorization from NASD's Chairman and CEO or NASD's Senior Executive Vice President for Regulatory Policy and Programs [the President of NASD Regulatory Policy and Oversight or the Executive Vice President for NASD Regulatory Policy and Programs]—may issue a notice to such member or person stating that the failure to comply with the temporary or permanent cease and desist order within seven days of service of the notice will result in a suspension or cancellation of membership or a suspension or bar from associating with any member.

(b) through (h) No Change.

* * * * *

9800. Temporary Cease and Desist Orders

(The entire Rule 9800 Series, and related amendments adopted by SR-NASD-98-80 to Rule 8310, IM-8310-3(c)(1) (formerly IM-8310-2(d)(1), renumbered by SR-NASD-2003-168), 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, [2007]2009, unless extended or permanently adopted by the Association pursuant to SEC approval at or before such date.)

9810. Initiation of Proceeding

(a) Department of Enforcement or Department of Market Regulation

With the prior written authorization of NASD's Chairman and CEO or NASD's Senior Executive Vice President for Regulatory Policy and Programs [the President of NASD Regulatory Policy and Oversight or the Executive Vice President for NASD Regulatory Policy and Programs], the Department of Enforcement or the Department of Market Regulation may initiate a temporary cease and desist proceeding with respect to alleged violations of Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 thereunder; SEC Rules 15g-1 through 15g-9; NASD Rule 2110 (if the alleged violation is unauthorized trading, or misuse or conversion of customer assets, or based on violations of Section 17(a) of the Securities Act of 1933); NASD Rule 2120; or NASD Rule 2330 (if the alleged violation is misuse or conversion of customer assets). The Department of Enforcement or the Department of Market Regulation shall initiate the proceeding by serving a notice on a member or associated person (hereinafter "Respondent") and filing a copy thereof with the Office of Hearing Officers. The Department of Enforcement or the Department of Market Regulation shall serve the notice by personal service, overnight commercial courier, or facsimile. If service is made by facsimile, the Department of

Enforcement or the Department of Market Regulation shall send an additional copy of the notice by overnight commercial courier. The notice shall be effective upon service.

(b) through (c) No Change.

* * * * *

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 Rule 9556.

NASD's Chairman and CEO or NASD's Senior Executive Vice President for Regulatory Policy and Programs [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.

* * * * *

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.⁵ The pilot program also gave NASD authority to enforce cease and desist orders. In June 2005, NASD extended the pilot program for an additional two-year period.⁶ The current two-year pilot expires on June 23, 2007. NASD is proposing a rule change to extend the pilot program for an additional two-year period, to June 23, 2009. Such an extension will enable NASD to continue to issue and enforce temporary and permanent cease and desist orders. NASD's authority to issue TCDOs will 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 is seeking only to extend the pilot program period and make technical changes to the titles of the NASD executives who can authorize the initiation of cease and desist proceedings and 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 the program should continue and whether certain specific provisions 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

⁵ See Securities Exchange Act Release No. 47925 (May 23, 2003), 68 FR 33548 (June 4, 2003) (SR-NASD-98-80).

⁶ See Securities Exchange Act Release No. 51860 (June 16, 2005), 70 FR 36427 (June 23, 2005) (SR-NASD-2005-061).

customer funds improperly.⁷ 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.

The proposed extension of the pilot program for an additional two years will 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 will 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 two years.

The proposed rule change will become effective upon filing, will be operative on June 23, 2007, and will expire on June 23, 2009, unless extended or permanently adopted by NASD pursuant to Commission approval at or before such date.

⁷ See Securities Exchange Act Release No. 51270 (February 28, 2005) (summarizing NASD's cease and desist proceedings against former NASD member L.H. Ross & Company).

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁸ 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 proposed rule change also is consistent with the provisions of Section 15A(b)(7) of the Act,⁹ 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. 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 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

⁸ 15 U.S.C. 78o-3(b)(6).

⁹ 15 U.S.C. 78o-3(b)(7).

as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁰ and Rule 19b-4(f)(6) thereunder.¹¹

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.

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. Please include File Number SR-NASD-2007-033 on the subject line.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASD-2007-033. 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

¹⁰ 15 U.S.C. 78s(b)(3)(A).

¹¹ 17 CFR 240.19b-4(f)(6).

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 office of 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-2007-033 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹²

Florence E. Harmon
Deputy Secretary

¹² 17 CFR 200.30-3(a)(12).