

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54279; File No. SR-NASD-2006-070)

August 7, 2006

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Approving a Proposed Rule Change to Amend the Safe Harbor For Business Expansions

On June 2, 2006, the National Association of Securities Dealers, Inc. (“NASD”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend NASD Interpretative Material 1011-1 (Safe Harbors for Business Expansions) (“IM-1011-1”) to limit the types of violations of Rule 2110 (Standards of Commercial Honor and Principles of Trade) that would result in a member being ineligible to use the safe harbor for business expansions and to make certain technical changes.³ The proposed rule change was published for comment in the Federal Register on July 5, 2006.⁴ The Commission received no comments on the proposal. This order approves the proposed rule change.

The Commission finds that the proposed rule change is consistent with Section 15A of the Act⁵ and the rules and regulations thereunder.⁶ Specifically, the Commission

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ The safe harbor permits a member to expand its business operations without having to submit an application pursuant to Rule 1017 to receive NASD approval before acting.

⁴ See Securities Exchange Act Release No. 54051 (June 27, 2006), 71 FR 38194 (SR-NASD-2006-070).

⁵ 15 U.S.C. 78o-3.

⁶ In approving this proposed rule change the Commission has considered the proposed rule’s impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

finds the proposal to be consistent with Section 15A(b)(6) of the Act,⁷ in that it is designed to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The NASD has stated that when a member or individual is charged with violating an NASD rule, NASD frequently charges a violation of Rule 2110 as part of NASD's action. Thus, the inclusion of Rule 2110 in IM-1011-1, without any limitation, often results in members being ineligible to use the safe harbor if they (or any of their principals) have violated any other NASD rule, which was not the intended effect. The proposed rule change would deem a member ineligible to use the safe harbor only where the finding of a violation of Rule 2110 by the member or a principal of the member raises significant investor protection issues because the violation involves unauthorized trading, churning, conversion, material misrepresentations or omissions to a customer, front-running, trading ahead of research reports, or excessive markups.⁸ Limiting the types of violations of Rule 2110 that constitute "disciplinary history" for purposes of IM-1101-1 would allow additional firms to rely on the safe harbor, consistent with the original intent of the safe harbor provision and the promotion of just and equitable principles of trade, while at the same time ensuring the protection of investors and the public interest by deeming a member ineligible to use the safe harbor where the

⁷ 15 U.S.C. 78o-3(b)(6).

⁸ A member would not be eligible to rely on the safe harbor for material changes in business operations if the member or any of its principals have been found, within the past five years, to have violated Rule 2110 in the context of one or more of these enumerated activities (or to have violated any of the other rules specified in IM-1011-1). The proposed limits on violations of Rule 2110 mirror the limits on Rule 2110 with respect to the public release of disciplinary complaints. See IM-8310-2 (Release of Disciplinary and Other Information Through BrokerCheck) and the related Notice to Members 97-42 (July 1997).

violation of Rule 2110 by the member or a principal presents significant investor protection issues.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁹ that the proposed rule change (SR-NASD-2006-070), be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁰

Nancy M. Morris
Secretary

⁹ 15 U.S.C. 78s(b)(2).

¹⁰ 17 CFR 200.30-3(a)(12).