

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-50456; File No. SR-NASD-2004-098)

September 27, 2004

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Approving Proposed Rule Change and Amendment No. 1 Thereto Relating to Proposed Amendments to Eliminate Exemptions from the Continuing Education Regulatory Element Requirements

On June 25, 2004, the National Association of Securities Dealers (“NASD”) filed with the Securities and Exchange Commission (“Commission” or “SEC”) a proposed rule change, 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> to eliminate all currently effective exemptions from the requirement to complete the Regulatory Element of the Continuing Education (“CE”) Program. On July 23, 2004, NASD submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The proposed rule change, as amended, was published for comment in the Federal Register on August 23, 2004.<sup>4</sup> The Commission received no comments on the proposal. This order approves the proposed rule change, as amended.

NASD Rule 1120(a) currently provides, in part, that no member shall permit any registered person to continue to, and no registered person shall continue to, perform duties as a registered person, unless such person has complied with the Regulatory Element of the CE requirement set forth in this Rule.<sup>5</sup> The Regulatory Element component of NASD Rule 1120(a)(1) requires each registered person to complete a standardized, computer-based,

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

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

<sup>3</sup> See letter from Grace Yeh, Assistant General Counsel, NASD, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission, dated July 22, 2004 (“Amendment No. 1”). In Amendment No. 1, NASD replaced in its entirety the original rule filing.

<sup>4</sup> See Securities Exchange Act Release No. 50204 (August 16, 2004), 69 FR 51873 (August 23, 2004).

<sup>5</sup> See NASD Rule 1120(a)(1).

interactive CE program within 120 days of their second registration anniversary date and every three years thereafter, or as otherwise prescribed by NASD. Registered persons who fail to complete the Regulatory Element are deemed inactive and may not perform in any capacity or be compensated in any way requiring registration.

Currently, two classes of persons are exempt from Regulatory Element requirements under NASD Rule 1120(a). The first class of persons come within the “grandfathered” exemption which applies to persons who were continuously registered, without serious disciplinary action,<sup>6</sup> for more than ten years as of the Rule’s effective date (i.e., July 1, 1995). The second class of persons come within the “graduated” exemption, which, although discontinued as of July 1998, continues to apply to registered persons who were “graduated” prior to the discontinuation of the exemption.<sup>7</sup>

However, in response to recommendations made by the Securities Industry/Regulatory Council on Continuing Education (the “Council”), NASD submitted a proposed rule change to eliminate all currently effective exemptions from required participation in Regulatory Element

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<sup>6</sup> For purposes of NASD Rule 1120, a significant disciplinary action generally means a statutory disqualification as defined in Section 3(a)(39) of the Act; a suspension or imposition of a fine of \$5,000 or more; or being subject to an order from a securities regulator to re-enter the Regulatory Element. See Rule 1120(a)(3).

<sup>7</sup> When NASD Rule 1120 was first adopted in 1995, the Regulatory Element schedule required registered persons to satisfy the Regulatory Element on the second, fifth, and tenth anniversary of their initial securities registration. After satisfying the tenth anniversary requirement, a person was “graduated” from the Regulatory Element. A graduated principal re-entered the Regulatory Element if he or she incurred a significant disciplinary action. A graduated person who was not a principal re-entered if he or she acquired a principal registration or incurred a significant disciplinary action.

programs.<sup>8</sup> The Council believes that there is great value in exposing all registered industry participants to the full benefit of Regulatory Element programs.

NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 60 days following Commission approval. Proposed amendments are expected to become effective (1) not more than 30 days following publication of the Notice to Members announcing Commission approval, (2) not more than 30 days following the implementation of necessary changes to Web Central Registration Depository (“Web CRD”), or (3) April 4, 2005, whichever date is latest to occur.

The Commission finds that the proposed rule change, as amended, is consistent with the requirements of Section 15A of the Act,<sup>9</sup> and the rules and regulations thereunder applicable to a national securities association.<sup>10</sup> In particular, the Commission finds that the proposed rule change is consistent with Section 15A(b)(6) of the Act,<sup>11</sup> which requires, among other things, that the Association’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. The Commission believes that the proposed rule change should help to ensure that all registered persons are kept up-to-date on regulatory, compliance, and sales practice-related industry issues. Further, the Commission believes that the proposed rule change will reinforce the importance of compliance

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<sup>8</sup> The Council recommended at its December 2003 meeting that SRO Rules (e.g., NASD Rule 1120(a)), be amended to eliminate existing exemptions from the Regulatory Element and to require all “grandfathered” and “graduated” persons to fully participate in future standardized CE programs, according to the Rule’s prescribed schedule.

<sup>9</sup> 15 U.S.C. 78o-3.

<sup>10</sup> In approving the proposed rule change, the Commission has considered its impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>11</sup> 15 U.S.C. 78o-3(b)(6).

with just and equitable principles of trade by exposing all registered industry participants to the full benefits of the Regulatory Element programs, which include a new Regulatory Element module that focuses specifically on ethics.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>12</sup> that the proposed rule change (SR-NASD-2004-098), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>13</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>12</sup> 15 U.S.C. 78s(b)(2).

<sup>13</sup> 17 CFR 200.30-3(a)(12).