

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-52176; File No. SR-NASD-2005-086)

July 29, 2005

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Article VIII of the By-Laws of NASD Regulation, Inc. Relating to District Committees and District Nominating Committees

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 July 5, 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 and II below, which items have been prepared by NASD. NASD has filed the proposed 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.<sup>5</sup> 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 proposes to amend Article VIII (District Committees and District Nominating Committees) of the By-Laws of NASD Regulation, Inc. ("By-Laws") to clarify the qualification requirements for candidates to NASD District Committees and

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

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

<sup>5</sup> As required under Rule 19b-4(f)(6)(iii), NASD provided the Commission with written notice of its intent to file the proposed rule change at least five business days prior to the filing date.

District Nominating Committees (collectively, “Committees”), and to establish procedures for the nomination and election of an alternate candidate who will replace, in an uncontested election, a candidate nominated by the District Nominating Committee that withdraws from further consideration or is determined to be ineligible. Below is the text of the proposed rule change.<sup>6</sup> Proposed new language is italicized; proposed deleted text is [bracketed].

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## ARTICLE VIII

### DISTRICT COMMITTEES AND DISTRICT NOMINATING COMMITTEES

**Sec. 8.1** No change.

#### **Composition of District Committees**

**Sec. 8.2** (a) A district created under Section 8.1 shall elect a District Committee pursuant to this Article. A District Committee shall consist of no fewer than five and no more than 20 members, unless otherwise provided by resolution of the Board. Subject to the limitation set forth in the immediately preceding sentence, the authorized number of members of a District Committee shall be determined from time to time by the Board; provided, however, that no decrease in the authorized number of members of a District Committee shall shorten the term of office of any member thereof. Each District Committee member shall: (1) be [employed by] registered with an NASD member

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<sup>6</sup> The Commission made minor technical changes to the rule text on behalf of the NASD. See E-mail from Kosha Dalal, Associate General Counsel, NASD, to Ronesha A. Butler, Special Counsel, Division of Market Regulation, Commission, dated July 27, 2005.

eligible to vote in the district for District Committee elections, and (2) work primarily from such NASD member's principal office or a branch office that is located within the district where the member serves on a District Committee. Members of the District Committees shall serve as panelists in disciplinary proceedings in accordance with the Rules of the Association. The District Committees shall consider and recommend policies and rule changes to the Board. The District Committees shall endeavor to educate NASD members and other brokers and dealers in their respective districts as to the objects, purposes, and work of the NASD and NASD Regulation in order to foster NASD members' interest and cooperation.

**Sec. 8.3 to Sec. 8.8.** No change.

### **Composition of District Nominating Committees**

**Sec. 8.9 (a)** Each district created under Section 8.1 shall elect a District Nominating Committee pursuant to this Article. A District Nominating Committee shall consist of five members, unless the Board by resolution increases a District Nominating Committee to a larger number. Each District Nominating Committee member shall: (1) be [employed by] registered with an NASD member eligible to vote in the district for District Committee elections, and (2) work primarily from such NASD member's principal office or a branch office that is located within the district where the member serves on a District Nominating Committee, but shall not be a member of the District Committee. A majority of the members of the District Nominating Committee shall include persons who previously have served on a District Committee or who are current or former Directors or current or former Governors of the NASD Board.

**Sec. 8.10 to Sec. 8.16.** No change

### **District Nominating Committee Slate**

**Sec. 8.17 (a)** The District Nominating Committee shall review the background of proposed candidates and the description of the NASD membership provided by NASD Regulation staff and shall nominate a slate of candidates for the election. The slate shall include one candidate for each open position on the District Committee and the District Nominating Committee subject to election at the next annual election. The District Nominating Committee may also nominate one alternate candidate for the District Committee and one alternate candidate for the District Nominating Committee. In the event of an uncontested election pursuant to Section 8.19, the alternate candidate would replace any member of the nominated slate of candidates who withdrew or was determined to be ineligible. In nominating candidates for the office of member of the District Committee and the office of member of the District Nominating Committee, the District Nominating Committee shall endeavor to secure appropriate and fair representation on the District Committee and on the District Nominating Committee of the various sections of the district and various classes and types of NASD members engaged in the investment banking or securities business within the district. In nominating candidates for the office of member of the District Nominating Committee, a District Nominating Committee shall assure that the composition of the District Nominating Committee meets the standards in Section 8.9(a).

## **Notification of Nomination**

**Sec. 8.18** The District Director, acting on behalf of the District Nominating Committee, shall give a Notice to the Secretary of NASD Regulation of each candidate nominated by the District Nominating Committee and the office to which the candidate is nominated. If the District Nominating Committee chooses, in its discretion, to nominate an alternate candidate for either the District Committee or the District Nominating Committee, or an alternate candidate for each such Committee, the District Director shall give Notice to the Secretary of NASD Regulation of each alternate candidate nominated by the District Nominating Committee and the office to which each alternate candidate is nominated. On or before October 1 of each year, the Secretary of NASD Regulation shall give a Notice of the nominated candidates and any alternate candidate(s) to the Executive Representatives of NASD members and the District Committee.

**Sec. 8.19.** No change

## **Designation of Additional Candidates**

**Sec. 8.20** If an officer[,]or director[,]of, or [employee of]individual who is registered with, an NASD member who meets the qualifications of Section 8.2 or 8.9, as applicable, is not nominated by the District Nominating Committee as a candidate or an alternate and wants to be considered for election to the District Committee or the District Nominating Committee, he or she shall deliver a written notice to the District Director within 14 calendar days after the Secretary of NASD Regulation gives the Notice of nominated candidates pursuant to Section 8.18. The District Director shall make a written record of the time and date of the receipt of the officer's, director's, or

[employee's]registered person's notice. The officer, director, or [employee]registered person shall be designated as an "additional candidate."

**Sec. 8.21 to Sec. 8.33** No change

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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

The By-Laws set forth provisions relating to the operation of the Committees, including specifically, provisions regarding Committee meetings, vacancies and elections. Under Article VIII, the role of the District Committee members includes serving as panelists in disciplinary proceedings in accordance with NASD Rules, recommending policy and rule changes to the Board, educating members in their district, and selecting members of the regional Committees in a manner consistent with the By-Laws. The role of the District Nominating Committee includes nominating candidates to serve on the Committees for that region. Currently, there are 11 District Committees, divided by geographic region. The By-Laws set forth provisions governing the annual elections of the Committees.

In the 2004 District Committee election, potential candidates sought clarification of the qualification requirements set forth in Article VIII, Sections 8.2 and 8.9 of the By-Laws. Specifically, questions arose as to the meaning of the language in such Sections requiring that potential candidates for election to, respectively, a District Committee or District Nominating Committee, be “employed by” a member eligible to vote in that district. To clarify the term, NASD is proposing to replace these references in Sections 8.2 and 8.9, and the reference to “employee” in Section 8.20, with the term “registered with” and “registered person,” respectively, thereby making it clear that any person associated and registered with the member is eligible for election to the District Committee or District Nominating Committee irrespective of whether such person is, as a legal matter, employed by such member.<sup>7</sup>

In addition, in the 2004 District Committee election, a candidate nominated by the District Nominating Committee for District 10 withdrew from further consideration following the September 2004 Special Notice to Members announcing the nominees for District 10 and prior to the distribution of the contested election ballot. As a result, procedures were implemented to allow the District Nominating Committee for District 10

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<sup>7</sup> Any person who engages in the investment banking or securities business of a member must be registered with NASD and be an associated person of that member. There is no requirement that associated persons be employees. They may, in fact, operate for employment law purposes as independent contractors. The Commission reiterates its longstanding position that the designation of independent contractor has no relevance for purposes of the securities laws. See letter to Gordon S. Macklin, President, NASD from Douglas Scarff, Director, Division of Market Regulation, dated June 18, 1982. NASD believes the requirement of being “registered with” as opposed to “employed by” the member more accurately aligns the candidacy requirements with the qualification of persons who may represent a member.

to amend the slate of nominees to include an alternate nominee to replace the withdrawing nominee.

To add flexibility to the nomination process and avoid potential delays, NASD is proposing to amend Section 8.17(a) to permit the District Nominating Committee, at the time it nominates its slate of candidates for the District Committee and the District Nominating Committee, to identify one alternate candidate for each such Committee. The alternate candidate would, in the context of an uncontested election, replace a nominated candidate who withdraws or is otherwise determined to be ineligible. In addition, NASD is proposing to amend Section 8.17(a) to provide that in an uncontested election, if any of the nominees for the District Committee or the District Nominating Committee withdraws or is determined to be ineligible before being declared duly elected, the withdrawing/ineligible nominee would be replaced by the alternate candidate. In an uncontested election, candidates are deemed duly elected 14 days after the Secretary of NASD Regulation provides notice of the nominated candidates to the Executive Representatives of NASD members and the District Committee and, so long as no additional candidate has come forward pursuant to Section 8.20 of the By-Laws. If a Committee member withdraws after the Committee members are duly elected, the vacancy provisions of the By-Laws, Sections 8.4 and 8.11, would apply. The proposed amendments to the By-Laws contemplate that an alternate candidate will replace a candidate on the slate only when an election is uncontested.



## 2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,<sup>8</sup> in general, and with Section 15A(b)(6) of the Act,<sup>9</sup> in particular, which require, among other things, that NASD 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.

### 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

Because the foregoing proposed 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 Act<sup>10</sup> and Rule 19b-4(f)(6)<sup>11</sup> thereunder.

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<sup>8</sup> 15 U.S.C. 78o-3.

<sup>9</sup> 15 U.S.C. 78o-3(b)(6).

<sup>10</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>11</sup> 17 CFR 240.19b-4(f)(6).

A proposed rule change filed under Rule 19b-4(f)(6)<sup>12</sup> normally does not become operative prior to thirty days after the date of filing. NASD requests that the Commission waive the 30-day operative delay, as specified in Rule 19b-4(f)(6)(iii), and designate the proposed rule change to become operative immediately to allow the proposed rule change to be operative before the start of the 2006 Committees' election cycle. The Commission hereby grants the request. The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because the waiver will allow the NASD to clarify and streamline the election processes governing the Committees and clarify the qualification requirements of candidates to serve on a District Committee or District Nominating Committee for the 2006 election cycle.<sup>13</sup> For these reasons, the Commission designates the proposed rule change as effective and operative immediately.

At any time within 60 days of the filing of the proposed rule change the Commission may summarily abrogate such proposed 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:

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<sup>12</sup> Id.

<sup>13</sup> For purposes only of waiving the operative delay for this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

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 SR-NASD-2005-086 on the subject line.

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 SR-NASD-2005-086. 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 office 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 SR-NASD-2005-086 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.<sup>14</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>14</sup> 17 CFR 200.30-3(a)(12).