

**IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION**

NEIL J. ASLIN, individually and on)	
behalf of all others similarly situated,)	
)	
Plaintiff,)	
)	Case No.
v.)	
)	
Financial Industry Regulatory)	
Authority, Inc., a Delaware)	
not-for-profit corporation,)	
)	
Defendant.)	

COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

NOW COMES Plaintiff, Neil J. Aslin (“Aslin”), individually and on behalf of all others similarly situated, by and through his undersigned attorney, and for his complaint against the Defendant, Financial Industry Regulatory Authority, Inc. (“FINRA”), a Delaware not-for-profit corporation, states as follows:

JURISDICTION AND VENUE

1. Plaintiff is, and at all times relevant hereto was, a citizen of the State of Illinois.
2. FINRA is a Delaware not-for-profit corporation with its principal place of business in New York City, New York and with offices in Chicago, Illinois.
3. This is an action arising out of the laws of the United States of America and involves a federal question and, therefore, this Court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. § 1331.

4. The acts and omissions herein alleged occurred in Chicago, Illinois, and, therefore, venue is properly before the United States District Court for the Northern District of Illinois, Eastern Division.

CLASS ALLEGATIONS

5. Plaintiff brings this case as a class action pursuant to Federal Rule of Civil Procedure (F.R.C.P.) 23, on behalf of himself and all others similarly situated.

6. The members of the class (“the Class”) are all persons currently registered with FINRA who were registered or employed with a broker/dealer that FINRA has designated as a “Disciplined Firm” pursuant to Rule 3010(b)(2)(J).

7. Upon information and belief, the members of the Class exceed five hundred.

8. Plaintiff will fairly and adequately represent and protect the interests of the Class. Plaintiff is knowledgeable concerning the subject matter of this action, has retained counsel competent and experienced in complex class actions, and intends to vigorously prosecute this litigation.

9. Plaintiff is aware of no conflicts of interest between himself and absent Class members.

10. Common questions of law and fact exist as to the claims of all Class members.

11. The aforementioned common questions of law and fact predominate over any questions that may affect individual Class members.

12. The common questions of law or fact include, but are not limited to, the following:

- a. Whether the promulgation of FINRA Rule Rule 3010(b)(2) and its approval by the Securities and Exchange Commission (“S.E.C.”) constitutes governmental action;
- b. Whether the imposition of the taping requirements of Rule 3010(b)(2)(H) merely because registered persons who had previously been associated with a “Disciplined Firm” is a denial of due process under the Fifth Amendment to the Constitution of the United States to such registered persons who were not involved in the activities that led to their former broker/dealer being designated a “disciplined firm” pursuant to FINRA Rule 3010(b)(2)(J); and
- c. Whether FINRA must provide a mechanism for a registered person to establish that he or she was not involved in any of the activities that led to FINRA designating the registered person’s former broker/dealer as a disciplined firm pursuant to Rule 3010(b)(2)(J).

13. The claims of Plaintiff are typical of those of the proposed Class.

14. The common questions of law and fact described above predominate over any individual issues that may affect any Class member.

15. A class action is superior to other means for the fair and efficient adjudication of the controversy for the following reasons, among others:

- a. Plaintiff is not aware of pending litigation by or against Class members with respect to the remedies sought in this action;
- b. The trial of a multiplicity of individual actions would cause a wasteful depletion of the limited resources of the courts and litigants, whereas concentrating the litigation of many identical claims in one forum is desirable and in the interests of judicial economy and efficiency;
- c. The Court may define the Class and create subclasses as may be necessary or desirable to adjudicate common issues and claims of the Class members; and
- d. Plaintiff does not know of any difficulties likely to be encountered in the management of this litigation that preclude its maintenance as a class action, particularly since FINRA knows the identity of all Class members and has in its possession the records necessary to provide the Class members’ damages.

THE REGULATORY STRUCTURE

16. The Securities Exchange Act of 1934, 15 U.S.C. §§ 78a *et seq.* (Exchange Act), provides a comprehensive system of federal regulation of the securities industry.

17. The Maloney Act, Pub. L. No. 75-719, 52 Stat. 1070 (1938) (amending the Exchange Act, 15 U.S.C. §§ 78o *et seq.*), established extensive guidelines for the formation and oversight of self-regulatory organizations, such as FINRA.

18. Congress delegated power to these organizations to enforce, at their own initiative, compliance by members of the industry with the requirements laid down in the Exchange Act and the regulations promulgated thereunder.

19. Pursuant to the Maloney Act, any association of securities broker-dealers seeking to register as a "national securities association" must file with the S.E.C. an application for registration ... containing the rules of the association." 15 U.S.C. §§ 78o-3(a). Furthermore, an association must "comply with the [Exchange Act] and its own rules," *id.* § 78s(g)(1)(A), and must "enforce compliance ... by its members and persons associated with its members," *id.*; *see also* 15 U.S.C. Sec. 78s(h).

20. Although a national securities association is a self-regulatory entity, it remains subject to the S.E.C.'s oversight and control. *Id.* § 78s(b). FINRA is subject to extensive oversight, supervision, and control by the S.E.C. on an ongoing basis. 15 U.S.C. Sec. 78s(a)(3)(B). For example, any proposed change in the association's rules must be filed with the S.E.C. and no proposed rule change can take effect unless approved by the SEC. *Id.* § 78s(b)(1).

21. Furthermore, the S.E.C. may abrogate, add to, and delete from the rules of a self-regulatory organization as the S.E.C. deems necessary or appropriate to insure the fair

administration of the self-regulatory organization or to conform its rules to requirements of the federal securities laws. *Id.* § 78s(c).

22. FINRA, as the successor of the National Association of Security Dealers (“NASD”), is the only officially registered “national securities association” under the Exchange Act.

23. FINRA wears two institutional hats: it serves as a professional association, promoting the interests of its members and acting as a quasi-governmental agency, with express statutory authority to adjudicate actions against members who are accused of violating the Exchange Act and/or S.E.C. regulations. See 15 U.S.C. § 78o-3(b)(7)).

24. Registered representatives such as the Plaintiff are required to register with FINRA and are subject to its rules.

25. All broker/dealers are required to register with FINRA and are, likewise, subject to its rules.

26. When FINRA promulgates and enforces its rules, FINRA is acting in a quasi-governmental capacity with the full force and authority of the United States Government and its actions in so doing are, therefore, governmental actions and, as such, are subject to the constraints imposed by the Due Process Clause of the Fifth Amendment to the Constitution of the United States.

27. The Maloney Act specifies certain procedural safeguards for the self-regulatory organization's disciplinary process. *See e.g.* 15 U.S.C. Sec. 78o -3(h)(1).

28. FINRA, acting as delegated quasi-governmental regulatory authority has promulgated (and the S.E.C. has approved) Rule 3010(b)(2) (formerly NASD Rule 3010(b)(2)) whereby registered representatives, even though not involved in any wrong-doing are

stigmatized and denied the value of their FINRA registration, their expertise, and their work product without due process of law.

FINRA RULE 3010(b)(2)

29. FINRA Rule 3010(b)(2) provides that when a member firm (*i.e.* broker/dealer) “is notified by NASD or otherwise has actual knowledge that it meets one of the criteria in paragraph (b)(2)(H) relating to the employment history of its registered persons at a Disciplined Firm as defined in paragraph (b)(2)(J) shall establish, maintain, and enforce special written procedures for supervising the telemarketing activities of *all* of its registered persons” (emphasis supplied).

30. FINRA has a rule imposing the following supervisory requirement on its members:

The following members shall be required to adopt special supervisory procedures over the telemarketing activities of their registered persons:

- A firm with at least five but fewer than ten registered persons, where 40% or more of its registered persons have been associated with one or more Disciplined Firms in a registered capacity within the last three years;
- A firm with at least ten but fewer than twenty registered persons, where four or more of its registered persons have been associated with one or more Disciplined Firms in a registered capacity within the last three years;
- A firm with at least twenty registered persons, where 20% or more of its registered persons have been associated with one or more Disciplined Firms in a registered capacity within the last three years.

For purposes of the calculations required in subparagraph (H), firms should not include registered persons who:

- (1) have been registered for an aggregate total of 90 days or less with one or more Disciplined Firms within the past three years; and
- (2) do not have a disciplinary history.

FINRA Rule 3010(b)(2)(H).

31. A “Disciplined Firm” is defined by FINRA as:

For purposes of this Rule, the term "disciplined firm" means either a member that, in connection with sales practices involving the offer, purchase, or sale of any security, has been expelled from membership or participation in any securities industry self-regulatory organization or is subject to an order of the Securities and Exchange Commission revoking its registration as a broker/dealer; or a futures commission merchant or introducing broker that has been formally charged by either the Commodity Futures Trading Commission or a registered futures association with deceptive telemarketing practices or promotional material relating to security futures, those charges have been resolved, and the futures commission merchant or introducing broker has been closed down and permanently barred from the futures industry as a result of those charges; or a futures commission merchant or introducing broker that, in connection with sales practices involving the offer, purchase, or sale of security futures is subject to an order of the Securities and Exchange Commission revoking its registration as a broker or dealer.

FINRA Rule 2010(b)(2)(J).

32. Whether an individual broker committed any wrongdoing is wholly irrelevant for the purposes of FINRA Rule 3010(b)(2)(H). The mere fact that the individual broker was registered with a “Disciplined Firm” taints the innocent, individual broker.

33. The individual broker who has been employed by the “Disciplined Firm” counts towards the percentage of brokers that a broker/dealer, pursuant to FINRA Rule 3010(b)(2)(H), is required to tape conversations with all current and prospective customers of that broker/dealer.

34. FINRA provides no mechanism whereby the broker who has been associated with a “disciplined” firm can establish that he or she had no involvement with the events that caused their previous employer to be designated a “Disciplined Firm.” Rule 3010(b)(2) is, therefore, a rule that applies a guilt-by-association stigma to all registered brokers of the “Disciplined Firm.”

35. The installation of a system to tape all telephone conversations with customers of a broker/dealer costs tens of thousands of dollars. Furthermore, implementation of special supervisory procedures as required by Rule 3010(b)(2) also adds to the costs of a broker/dealer who hires a broker from a Disciplined Firm if such a hiring places the broker/dealer above the

threshold number of registered representatives from “Disciplined Firms” as specified by FINRA Rule 3010(b)(2)(H).

36. As a result, the individual broker whose registration would exceed the percentage of brokers from one or more Disciplined Firms as set forth in FINRA Rule 3010(b)(2)(H) and who is denied the registration by a FINRA member firm because to hire him or her would raise the number of “tainted” brokers employed by the member firm to a level requiring mandatory taping of conversations and the implementation of special supervisory procedures, is a fundamental denial of due process and a deprivation of the individual’s property rights.

37. A rule, enforced by an agency of the United States Government, that places a taint upon an individual, regardless of whether that person has engaged in any type of illegal or otherwise sanctionable conduct, that deprives that individual of the ability to practice his or her vocation, is capricious and arbitrary.

38. FINRA provides no process by which a former registrant of a disciplined firm can remove the “taint” arbitrarily imposed by Rule 3010(b)(2).

39. A regulatory scheme that stigmatizes an individual without providing an articulated standard by which to determine if the individual bears any culpability for the actions that caused his or her broker dealer to be designated a “Disciplined Firm”, deprives such a registered individual of the right to practice his or her vocation with member firms who would otherwise agree to hire the broker but have refused to do so because such a hiring would trigger the taping and special supervisory system. This, in turn, constitutes a taking of property by a quasi-governmental agency without the benefit of fundamental due process safe guards.

PLAINTIFF'S SITUATION

40. Plaintiff first became registered with FINRA's predecessor, the NASD, in 1975. Eventually, Plaintiff registered with Brewer Financial Services, LLC ("Brewer Financial") in May of 2005.

41. Plaintiff left Brewer Financial in March of 2009 and became associated with BEST Direct Securities, LLC ("BEST Direct") in April of 2009.

42. BEST Direct is not a "Disciplined Firm" and has no disciplinary, financial or regulatory events. Nor have any customer complaints or arbitrations been filed against BEST Direct.

43. The only event on Plaintiff's CRD (the central registrar maintained by FINRA for registered representatives and member firms) is a 1988 consent and waiver for being a principal of a member firm that had a net capital violation.

44. The actions of Brewer Financial and its principals that formed the basis of the S.E.C. Complaint filed in the United States District Court for the Northern District of Illinois, Eastern Division, Case No. 10-cv-06932, alleged that the misconduct began in or around June of 2009, three months after Plaintiff left Brewer Financial.

45. Furthermore, the misconduct alleged by the S.E.C. in Case No. 10-cv-06932 involved promissory notes issued by FPA Limited, an Isle of Man company ("the FPA notes"). Plaintiff had no involvement with the issuance or sale of any of the FPA notes.

46. Nevertheless, on April 6, 2011, FINRA sent a notice (a copy of which is attached as Exhibit "A" hereto and incorporated by reference herein) to BEST Direct informing BEST Direct that, pursuant to what FINRA terms the "Taping Rule" (Rule 30110(b)(2)), BEST Direct had to either institute taping pursuant to the FINRA Rule or cut its work force or implement the

required taping:

In particular, the amendments permit firms, within 30 days after receiving notice that they are subject to the Taping Rule or obtaining actual knowledge that they are subject to the Rule (and have promptly notified the Department of Member Regulation that they are subject to the Rule) to reduce their staffing levels to fall below the threshold levels set forth in the Taping Rule and thus avoid its application. Please review *Notices to Members 02-61 and 05-46* for the requirements pertaining to this reduction.

If Best Direct Securities LLC has triggered application of the Taping Rule for the first time and elects to take advantage of the relief described above, Best Direct Securities LLC must notify the Department of Member Regulation within 30 days of receipt of this notice, and include in the notification the names and CRD numbers of the terminated individuals, the dates of termination, the total number of registered representatives **currently** associated with the firm, and a written representation by the firm that it will not rehire persons terminated to accomplish the staff reduction for a period of 180 days.

(Bold and emphasis in original)

47. The Plaintiff was one of individuals that was “counted” to make BEST Direct subject to the “taping rule.” *See* Exhibit “A” hereto.

48. BEST Direct thereafter terminated Plaintiff on May 4, 2011 for the sole purpose of avoiding the taping requirements of FINRA Rule 3010(b)(2).

49. BEST Direct has informed Plaintiff that if the “taint” regarding his association with a Disciplined Firm is removed or if he is not counted by FINRA as an individual under the “taping” requirement of FINRA Rule 3010(b)(2), BEST Direct would revoke Plaintiff’s termination.

50. On June 13, 2011, FINRA confirmed that an individual broker cannot challenge his or her inclusion as a “tainted” registrant on a FINRA notice to a member firm requiring said firm to either conform to the numerical limitations of FINRA Rule 3010(b)(2)(H) or to reduce its “staffing level.” *See* Affidavit of Jennifer Muchoney attached as Exhibit “B” hereto and incorporated by reference herein.

51 . As a result of the arbitrary and capricious actions of FINRA as herein previously alleged and the absence of any mechanism within the FINRA and S.E.C. regulatory scheme for Plaintiff to remove the stigma of having been registered with a “Disciplined Firm”, the Plaintiff has lost his position with BEST Direct and now is foreclosed from using his securities license with those firms who, if they hired, Plaintiff, would be subject to the “Taping Rule.”

52 . Plaintiff has a vested right in his securities license and registration. Plaintiff has committed no act that would cause him to be personally censured, fined, expelled, or otherwise disciplined by FINRA or the S.E.C.

53 . As a direct and proximate cause of FINRA’s arbitrary and capricious action in naming him as a former associate or registrant of a “Disciplined Firm”, even though Plaintiff committed no wrongdoing whatsoever, FINRA has deprived the Plaintiff of a valuable property right without due process of law in violation of the Fifth Amendment to the Constitution of the United States.

COUNT I

(Injunctive and Declaratory Relief)

54 . Plaintiff re-alleges paragraphs 1 thru 53, above, as though each is specifically set forth herein in this, Paragraph 54 of this Count I of the Complaint.

55 . An actual controversy concerning the application of FINRA Rule 3010(2)(b) exists between the Plaintiff and FINRA within the meaning of 28 U.S.C. §2201.

56 . As a result of FINRA’s application of FINRA Rule 3010(b)(2) as herein previously alleged, the Plaintiff is suffering irreparable harm.

57 . Plaintiff has no adequate remedy at law.

58 . The Plaintiff has a likelihood of success on the merits.

59. The prevention of the violation of the Plaintiffs and other Class Members constitutional rights outweighs any interest FINRA may have in continuing to violate the due process rights of the Plaintiff and members of the punitive class.

WHEREFORE, Plaintiff prays that the Plaintiff prays that this Court enter an order:

- A. Declaring the enforcement of FINRA Rule 3010(b)(2)(H) without the availability of a procedural process through which a registered person can contest the imposition of the taint of having been associated with a “Disciplined Firm” as defined by FINRA Rule 3010(b)(2)(J) is a violation of the Fifth Amendment right to due process of the Plaintiff and all others similarly situated;
- B. Enjoining FINRA from enforcing the taping requirements of FINRA Rule 3010(b)(2)(H) until FINRA implements a process whereby the Plaintiff and all others similarly situated may challenge their status as a “tainted” individual; and
- C. Any other relief that the Court deems proper and just.

Respectfully submitted,

/s/Nicholas P. Iavarone
Nicholas P. Iavarone, Esq.

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April 6, 2011

Via Overnight Federal Express [7969 5605 9781]

Mr. Steven Zakrzewski
Chief Compliance Officer
and Executive Representative
Best Direct Securities LLC
One Peregrine Way
Cedar Falls, IA 50613

Dear Mr. Zakrzewski:

FINRA is notifying Best Direct Securities LLC that as of April 1, 2011, it meets one of the criteria set forth in NASD Rule 3010(b)(2) (the "Taping Rule") and is now subject to the rule's provisions. ~~As part of the Taping Rule's requirements, Best Direct Securities LLC~~ must establish, maintain and enforce special written procedures for supervising the telemarketing activities of its registered persons within 60 days after its receipt of this letter. These procedures must include the implementation of a taping system that will record all conversations between Best Direct Securities LLC's registered persons and both existing and potential customers, and these procedures must remain in effect for at least three years. *Notice to Members 98-52* contains a copy of the Rule, as well as additional background information and guidance for developing the required special written procedures.

Please note that the Securities and Exchange Commission ("SEC") approved amendments to the Taping Rule, which are described in detail in *Notices to Members 02-61 and 05-46*. All firms that trigger application of the Taping Rule (for the first time), may obtain relief from the requirements by complying with the Taping Rule as modified by the amendments. In particular, the amendments permit firms, within 30 days after receiving notice that they are subject to the Taping Rule or obtaining actual knowledge that they are subject to the Rule (and have promptly notified the Department of Member Regulation that they are subject to the Rule) to reduce their staffing levels to fall below the threshold levels set forth in the Taping Rule and thus avoid its application. Please review *Notices to Members 02-61 and 05-46* for the requirements pertaining to this reduction.

If Best Direct Securities LLC has triggered application of the Taping Rule for the first time and elects to take advantage of the relief described above, Best Direct Securities LLC must notify the Department of Member Regulation within 30 days of receipt of this notice, and include in the notification the names and CRD numbers of the terminated individuals, the dates of termination, the total number of registered representatives currently associated with the firm, and a written representation by the firm that it will not rehire persons terminated to accomplish the staff reduction for a period of 180 days.

Mr. Steven Zakrzewski
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Please send this notification in a letter to the following address:

FINRA
Member Regulation Department
Sales Practice Policy
1735 K Street, NW
Washington, DC 20006
Attn: Ann-Marie Mason, Esq.

If Best Direct Securities LLC is not eligible for relief or does not elect to reduce its staffing level, it is required to complete and return the enclosed "Certification Regarding Special Written Supervisory Procedures For Compliance With NASD Rule 3010(b)(2)" (Certification Form) to the FINRA Kansas City Office by no later than 10 business days after the firm is required to implement the special supervisory procedures, including the installation of the taping system. Please take the time to fully and accurately complete the entire Certification Form, which is being requested pursuant to FINRA Rule 8210. If additional room is needed for comments, please respond on a separate sheet of paper and specifically reference the appropriate Certification Form section and question numbers.

As described in *Notice to Members 98-52*, Best Direct Securities LLC must also comply with federal and state statutes governing the tape recording of conversations, wiretapping, and electronic surveillance. In implementing the taping system required by the Taping Rule, it is Best Direct Securities LLC's responsibility to obtain appropriate legal advice to comply with federal and state laws.

Rule 3010(b)(2) also requires that for the three-year period during which the taping procedures are in effect, Best Direct Securities LLC must submit a quarterly written report on its supervision of the telemarketing activities of its registered persons. This is in addition to submitting the Certification Form. Best Direct Securities LLC must file the quarterly reports with the FINRA Kansas City Office by the 30th day of the month following the end of each calendar quarter.

Included with this letter is a listing of the individuals who were associated with Best Direct Securities LLC at open of business April 1, 2011, who were also associated with one or more Disciplined Firms within the prior three years. Also included is a copy of the current listing of firms designated as Disciplined Firms. For future reference, the list of Disciplined Firms and other information about the Taping Rule is available on the FINRA Web Site (www.finra.org) under "Industry Professionals, Enforcement, Disciplinary Actions, Taping Rule" or <http://www.finra.org/Industry/Enforcement/DisciplinaryActions/TapingRule/index.htm>.

Best Direct Securities LLC may request an exemption from the requirements of the Taping Rule by filing a written application pursuant to FINRA Rule 9610. In accordance with the SEC's release approving the Taping Rule, Member Regulation will exercise its discretion to grant an exemption only upon a clear showing that it is warranted. Best Direct Securities LLC has the burden of showing that it will be able to adequately supervise its registered persons without a taping system to monitor conversations with customers.

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The application should be filed with:

FINRA
Member Regulation Department
Sales Practice Policy
1735 K Street, NW
Washington, DC 20006
Attn: Ann-Marie Mason, Esq.

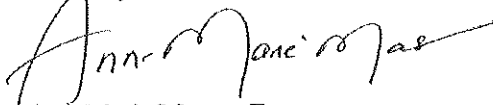
A copy of the application should be provided to:

FINRA
Office of General Counsel
Regulatory Policy and Oversight
1735 K Street, NW, 7th Floor
Washington, DC 20006-1506

This application must be received within 30 days of Best Direct Securities LLC's receipt of this notice.

Questions concerning compliance with the Taping Rule may be directed to Ann-Marie Mason, Principal Rule Counsel, at (202) 728-8231.

Sincerely,



Ann-Marie Mason, Esq.
Counsel, Sales Practice Policy
Member Regulation

Enclosures:

"Certification Regarding Special Written Supervisory Procedures For Compliance With NASD Rule 3010(b)(2)" form

Listing of Individuals Previously Employed by a Disciplined Firm (Taping Rule-Agent Concentration Information)

List of Disciplined Firms

Notice to Members 05-46

Notice to Members 02-61

Notice to Members 98-52

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cc: Scott DeArmey, Director
Kansas City District Office

Jennifer Luginbill, Associate Director
Kansas City District Office

Donald K. Lopezi, Deputy Director
Examination Programs Group

CERTIFICATION REGARDING SPECIAL WRITTEN SUPERVISORY PROCEDURES FOR COMPLIANCE WITH NASD RULE 3010(b)(2)

Firm Name: _____ CRD Number: _____

Pursuant to FINRA Rule 8210, this form must be filed with the appropriate FINRA District Office within ten business days of the date that the firm is required to implement the special supervisory procedures required by NASD Rule 3010(b)(2) (the "Taping Rule"). A copy of the firm's written supervisory procedures with respect to NASD Rule 3010(b)(2) must be attached to this form.

	YES	NO	COMMENTS/EXPLANATION
I. Effective Date			
Indicate the date that the firm implemented the required procedures, including the installation of a taping system.	<input type="checkbox"/>	<input type="checkbox"/>	
Please identify the person(s) responsible for implementing the required supervisory procedures and maintaining the recordings by name, title and CRD number.	<input type="checkbox"/>	<input type="checkbox"/>	
II. Recording System			
Please answer the following questions with respect to the firm's recording system for telephone conversations between registered persons and existing and potential customers:	<input type="checkbox"/>	<input type="checkbox"/>	
1. Does the system record all means of telecommunications at the firm?	<input type="checkbox"/>	<input type="checkbox"/>	
2. Does the system make audible recordings that can be understood when played back?	<input type="checkbox"/>	<input type="checkbox"/>	
3. Are the recordings cataloged and retained in accordance with the Taping Rule?	<input type="checkbox"/>	<input type="checkbox"/>	
4. Do the firm's registered persons have any control over the recording of conversations?	<input type="checkbox"/>	<input type="checkbox"/>	
5. Do the firm's registered persons have access to the recordings after they are stored?	<input type="checkbox"/>	<input type="checkbox"/>	

I certify that all information provided herein is true and accurate. Moreover, I understand that misrepresentations or omissions herein may subject me, my firm, or other persons associated with my firm, to disciplinary action and sanctions by FINRA.

Name and Title of Individual Completing Report _____ Telephone Number _____

Signature _____ Date _____

Name of Contact Person _____ Telephone Number _____



Industry Professionals - Enforcement - Disciplinary Actions

Taping Rule

Disciplined Firms Under NASD Taping Rule (NASD Rule 3010)

Effective August 17, 1998, the Securities and Exchange Commission approved an amendment to NASD Rule 3010 to require members to establish special supervisory procedures, including the tape recording of conversations, when they have hired more than a specified percentage of registered persons from certain firms that have been expelled or that have had their broker/dealer registrations revoked for violations of sales practice rules ("disciplined firms"). See Notice to Members 98-52 for a more specific explanation of this issue.

Below is a list of firms that meet the definition of "disciplined firm" under this Rule. This list is comprised of firms that were disciplined within the last three years.

Disciplined Firms

APS Financial Corporation
Aura Financial Services Inc
Barron Moore, Inc.
Brewer Financial Services, LLC
Dolphin & Bradbury Incorporated
K.W. Brown Investments
Meeting Street Brokerage, LLC
MICG Investment Management LLC
Mission Securities Corp
Mortgages LTD Securities, LLC
North American Clearing, Inc.
Provident Asset Management, LLC

Last Updated: 3/21/2011

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CRD® or IARD(TM) System - Current As Of 03/31/2011 11:40 PM
 Taping Rule - Agent Concentration Report
 CRD® or IARD(TM) System Report provided to: FINRA
 Request Submitted: 04/01/2011

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053
 FINRA District: 4KC

Number of approved FINRA individuals with this firm: 17
 Number of approved individuals from disciplined firms for this firm: 11
 Percentage of approved individuals from disciplined firms at this firm: 64.71 %

Individual Name: ABBANAT, GUY JAMES
 Individual CRD#: 1235698 SSN: 261-61-9141 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:

Category	Status	Effective Date
GS	APPROVED	01/25/2011
SU	APPROVED	01/25/2011

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558

Registrations:

Category	Start Date	End Date	Number of Days
GS	01/02/2009	11/05/2010	672
SU	01/02/2009	11/05/2010	672

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 01/02/2009
 Employment Type: RR
 End Date: 10/29/2010

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 01/02/2009
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: UBS FINANCIAL SERVICES INC.
 Firm CRD#: 8174
 Start Date: 06/30/2006
 Employment Type: RR/IAR
 End Date: 01/02/2009

Individual Name: ASLIN, NEIL JACKSON
 Individual CRD#: 814839 SSN: 499-38-2636 Billing Code:
 Has Relevant Disclosure: Y
 Occurrence ID: 300379
 Registrations:

Category	Status	Effective Date
GS	APPROVED	04/21/2009

CRD® or IARD(TM) System - Current As Of 03/31/2011 11:40 PM
 Taping Rule - Agent Concentration Report
 CRD® or IARD(TM) System Report provided to: FINRA
 Request Submitted: 04/01/2011

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053
 FINRA District: 4KC

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558

Registrations:

Category	Start Date	End Date	Number of Days
GS	05/12/2006	03/23/2009	1046

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 12/13/2005
 Employment Type: RR
 End Date: 03/23/2009

Individual Name: BROWN, STEPHEN MICHAEL
 Individual CRD#: 1221582 SSN: 511-56-9943
 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:

Category	Status	Effective Date
GP	APPROVED	12/22/2010
GS	APPROVED	12/22/2010

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558

Registrations:

Category	Start Date	End Date	Number of Days
GP	05/21/2009	11/05/2010	533
GS	05/21/2009	11/05/2010	533

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 05/21/2009
 Employment Type: RR
 End Date: 10/29/2010

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 05/21/2009
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: LPL FINANCIAL CORPORATION
 Firm CRD#: 6413
 Start Date: 07/28/1989
 Employment Type: RR/IAR
 End Date: 05/22/2009

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053 FINRA District: 4KC

Individual Name: CLARK, MS DEBRA JEAN
 Individual CRD#: 2668608 SSN: 576-56-5762 Billing Code:

Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:
 Category Status Effective Date
 GS APPROVED 12/22/2010

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558
 Registrations:
 Category Start Date End Date Number of Days
 GS 11/25/2008 11/05/2010 710

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558 Employment Type: RR
 Start Date 11/25/2008 End Date: 10/29/2010

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631 Employment Type: IAR
 Start Date 11/25/2008 End Date: 10/29/2010

Previous Firm: RAYMOND JAMES & ASSOCIATES, INC.
 Firm CRD#: 705 Employment Type: RR/IAR
 Start Date 12/02/2004 End Date: 11/26/2008

Individual Name: COCCARELLI, GUIDO ANTHONY
 Individual CRD#: 1899203 SSN: 163-40-2900 Billing Code:

Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:
 Category Status Effective Date
 GS APPROVED 01/25/2011

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558
 Registrations:
 Category Start Date End Date Number of Days
 GS 05/14/2010 11/05/2010 175

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558 Employment Type: RR
 Start Date 05/14/2010 End Date: 10/29/2010

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053
 FINRA District: 4KC

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 05/14/2010
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: AMERIPRISE FINANCIAL SERVICES, INC.
 Firm CRD#: 6363
 Start Date: 11/03/1988
 Employment Type: RR/IAR
 End Date: 05/14/2010

Individual Name: DALLAS, CHRISTOPHER T
 Individual CRD#: 3233864
 SSN: 354-54-9088
 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:

Category	Status	Effective Date
GP	APPROVED	01/25/2011
GS	APPROVED	01/25/2011

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558

Registrations:

Category	Start Date	End Date	Number of Days
GP	07/27/2010	11/04/2010	100
GS	07/27/2010	11/04/2010	100

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 07/27/2010
 Employment Type: RR
 End Date: 10/29/2010

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 07/27/2010
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: INTEROCEAN WEALTH MANAGEMENT LLC
 Firm CRD#: 140456
 Start Date: 02/08/2008
 Employment Type: IAR
 End Date: 01/30/2009

Previous Firm: INTEROCEAN SECURITIES LLC
 Firm CRD#: 141077
 Start Date: 02/08/2008
 Employment Type: RR
 End Date: 01/30/2009

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053
 FINRA District: 4KC

Individual Name: LISHCHYNSKY, JR MARK JOHN
 Individual CRD#: 2478952 SSN: 353-72-4536 Billing Code:
 Has Relevant Disclosure: Y
 Occurrence ID: 1398585, 1461654

Registrations:

Category	Status	Effective Date
GP	APPROVED	01/25/2011
GS	APPROVED	01/25/2011
OP	APPROVED	01/25/2011
SU	APPROVED	01/25/2011

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558
 Registrations:

Category	Start Date	End Date	Number of Days
IB	11/19/2009	11/04/2010	350
GP	03/19/2009	11/04/2010	595
GS	03/19/2009	11/04/2010	595
OP	03/19/2009	11/04/2010	595
SU	03/19/2009	11/04/2010	595

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 03/17/2009
 Employment Type: RR
 End Date: 10/29/2010

Previous Firm: INTEROCEAN SECURITIES LLC
 Firm CRD#: 141077
 Start Date: 04/01/2006
 Employment Type: RR
 End Date: 01/30/2009

Individual Name: MONTGOMERY, THOMAS EDWARD
 Individual CRD#: 5571240 SSN: 074-38-0948 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:

Category	Status	Effective Date
GS	APPROVED	12/22/2010

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053
 FINRA District: 4KC

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558

Registrations:

Category	Start Date	End Date	Number of Days
GS	06/12/2009	11/05/2010	511

Previous Firm: AMS ADVISORS LLC
 Firm CRD#: 142852
 Start Date: 11/05/2010
 Employment Type: IAR
 End Date: 12/31/2010

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 05/28/2009
 Employment Type: RR
 End Date: 10/29/2010

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 05/28/2009
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: BROOKSTONE CAPITAL MANAGEMENT LLC
 Firm CRD#: 141413
 Start Date: 07/23/2008
 Employment Type: IAR
 End Date: 05/27/2009

Individual Name: STOCKTON, SCOTT ALAN
 Individual CRD#: 2806750
 SSN: 449-51-1857
 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:

Category	Status	Effective Date
GS	APPROVED	02/11/2011

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558

Registrations:

Category	Start Date	End Date	Number of Days
GS	09/25/2009	11/05/2010	406

Previous Firm: AMS ADVISORS LLC
 Firm CRD#: 142852
 Start Date: 11/05/2010
 Employment Type: IAR
 End Date: 12/31/2010

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 09/25/2009
 Employment Type: RR
 End Date: 10/29/2010

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Firm Name: BEST DIRECT SECURITIES, LLC
 Firm CRD#: 146053
 FINRA District: 4KC

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 09/25/2009
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: AMERIPRISE FINANCIAL SERVICES, INC.
 Firm CRD#: 6363
 Start Date: 09/26/1996
 Employment Type: RR/IAR
 End Date: 09/25/2009

Individual Name: WOLF, JEFFREY ROBERT
 Individual CRD#: 2842614 SSN: 515-78-5768 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:
 Category Status Effective Date
 GS APPROVED 01/25/2011

Disciplined Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD #: 132558
 Registrations:

Category	Start Date	End Date	Number of Days
GS	09/25/2009	11/05/2010	406

Previous Firm: BREWER FINANCIAL SERVICES, LLC
 Firm CRD#: 132558
 Start Date: 09/25/2009
 Employment Type: RR
 End Date: 10/29/2010

Previous Firm: BREWER INVESTMENT ADVISORS LLC
 Firm CRD#: 134631
 Start Date: 09/25/2009
 Employment Type: IAR
 End Date: 10/29/2010

Previous Firm: AMERIPRISE FINANCIAL SERVICES, INC.
 Firm CRD#: 6363
 Start Date: 08/12/1997
 Employment Type: RR/IAR
 End Date: 09/25/2009

Individual Name: WYSE, ERIK LLOYD
 Individual CRD#: 2947140 SSN: 507-86-3958 Billing Code:
 Has Relevant Disclosure: N
 Occurrence ID:
 Registrations:
 Category Status Effective Date
 GS APPROVED 01/25/2011

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Firm Name:	BEST DIRECT SECURITIES, LLC	FINRA District:	4KC
Firm CRD#:	146053		
Disciplined Firm:	BREWER FINANCIAL SERVICES, LLC		
Firm CRD #:	132558		
Registrations:			
Category	Start Date	End Date	Number of Days
GS	05/07/2010	11/05/2010	182
Previous Firm:	BREWER FINANCIAL SERVICES, LLC		
Firm CRD#:	132558	Employment Type:	RR
Start Date	05/07/2010	End Date:	10/29/2010
Previous Firm:	BREWER INVESTMENT ADVISORS LLC		
Firm CRD#:	134631	Employment Type:	IAR
Start Date	05/07/2010	End Date:	10/29/2010
Previous Firm:	AMERIPRISE FINANCIAL SERVICES, INC.		
Firm CRD#:	6363	Employment Type:	RR/IAR
Start Date	09/09/1997	End Date:	05/07/2010

CRD® or IARD(TM) System Report -- See notice regarding CRD Data on cover page.

Notice to Members

SEPTEMBER 2002

SUGGESTED ROUTING

Executive Representatives
Legal & Compliance
Operations
Senior Management

INFORMATIONAL

Taping Rule

SEC Approves Proposed Changes to the Taping Rule and NASD Interpretive Material 8310-2; **Effective Date: October 14, 2002**

KEY TOPICS

Rule 3010
IM-8310-2
Taping Rule

Executive Summary

On August 28, 2002, the Securities and Exchange Commission (SEC) approved amendments to NASD Rule 3010(b)(2), also known as the Taping Rule, and NASD IM-8310-2. The amendments to the Taping Rule (1) permit firms that become subject to the Taping Rule a one time opportunity to adjust their staffing levels to fall below the prescribed threshold levels and thus avoid application of the Rule; (2) revise the criteria by which firms become subject to the Taping Rule by not including certain short-term employees of disciplined firms into the calculations of the Taping Rule threshold levels; (3) expand the compliance deadline from 30 to 60 days for firms subject to the Taping Rule to install taping systems; (4) clarify NASD's authority to grant exemptions from the Rule pursuant to the Rule 9600 Series only in exceptional cases; and (5) extend the taping requirements from two years to three years to eliminate conflicting time periods in the Taping Rule. In addition, the amendments to NASD IM-8310-2 permit, upon request, public disclosure of whether a particular firm is subject to the Taping Rule.

The amendments become effective on October 14, 2002. The text of the amendments to Rule 3010(b)(2) and IM-8310-2 is provided in Attachment A.

Questions/Further Information

Questions regarding this *Notice to Members* may be directed to Grace Yeh, Assistant General Counsel, Office of General Counsel, NASD Regulatory Policy and Oversight, at (202) 728-6939, or to Kyra Armstrong, Senior Attorney, Department of Member Regulation, NASD Regulatory Policy and Oversight, at (202) 728-6962.

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Discussion

The Taping Rule, which was adopted in 1998, is designed to ensure that members with a large number of registered persons from firms that have been expelled from membership or have had their registration revoked for sales practice violations (Disciplined Firms) have proper supervisory procedures over telemarketing activities to prevent fraudulent and improper sales practices or other customer harm. Under the Rule, firms that hire a significant number of employees from Disciplined Firms must establish, maintain, and enforce special written procedures for supervising the telemarketing activities of all their

registered persons. In addition, such firms are required to install taping systems to record all telephone conversations between all of their registered persons and both existing and potential customers, review the tape recordings, and file quarterly reports with NASD.

Generally, the amendments refine the application of the Taping Rule and provide additional flexibility to assist member firms in meeting their compliance obligations under the Rule.

1. *Establishment of a 30-Day Staff Adjustment Period*

The amendments provide all firms that, on or after October 14, 2002, trigger application of the Taping Rule (for the first time) a one-time opportunity to obtain relief from the Taping Rule requirements by adjusting their staffing levels.¹ In particular, the amendments permit firms, within 30 days after receiving the notice that they are subject to the Taping Rule or obtaining actual knowledge that they are subject to the Rule (and have promptly notified the Department of Member Regulation that

they are subject to the Rule), to reduce their staffing levels to fall below the threshold levels set forth in the Taping Rule and thus avoid application of the Taping Rule.² Firms will not be permitted to hire additional registered representatives to fall below the stated thresholds but rather will be required to reduce their number of registered representatives from Disciplined Firms. Once a firm has made the reductions, the firm will not be permitted to rehire the terminated individuals for a period of at least 180 days. Firms may elect, but are not required, to make reductions to their staffing levels. If a firm chooses not to make the adjustment, then it will be required to comply with the Taping Rule requirements.

A firm is permitted to adjust its staffing levels only when it becomes subject to the Taping Rule for the first time. If the firm re-triggers the Taping Rule at any point in the future, then the firm automatically will become subject to its provisions. While the amendments allow a new entity resulting from a restructuring (by a merger, acquisition, or otherwise) to make a staff adjustment to avoid application of the Taping Rule even if one of the participating members in the restructuring had previously adjusted its staff level pursuant to the amendments, this will not be the case for an entity that was restructured in an effort to avoid compliance with the Rule.

2. *Revision of the Criteria by Which Firms Become Subject to the Taping Rule*

The amendments revise the criteria for determining whether a firm is subject to the Taping Rule by excluding from the firm's calculations registered persons who were associated with a Disciplined Firm for only a short period of time.

Specifically, in calculating whether firms exceed the Taping Rule thresholds set forth in the Rule, registered persons who were registered with one or more Disciplined Firms for 90 days or less within the last three years and who have no disciplinary history by a finding of a violation of the provisions set forth in IM-1011-1, while still included in the total number of registered persons at a firm, may be excluded from the number of registered persons at the firm from Disciplined Firms. The amendments recognize that persons registered with Disciplined Firms for a short period of time (*i.e.*, an aggregate total of 90 days or less) are less likely to have acquired the "bad habits" from the Disciplined Firms that the Taping Rule seeks to redress.

In addition, the amendments clarify that the calculation of registered representatives from Disciplined Firms includes independent contractors previously registered with a Disciplined Firm.

3. Expansion of the Compliance Deadline from 30 to 60 Days

The amendments extend the period for firms to implement the special supervisory procedures, including the installation of taping systems from 30 days to 60 days of receiving notice from NASD (or obtaining actual knowledge) that they are subject to the Taping Rule. Based on NASD's experience, 60 days should provide adequate time for firms to install the taping systems and would alleviate the need for firms to request extensions of time. NASD notes that generally, an acceptable taping system would not include one where a firm's associated persons whose communications with customers are

required to be taped have control over the operation of, or the tape recordings produced from, the taping system.

4. Clarification of the Exemptive Relief Authority

The amendments clarify that NASD may grant exemptions from the Taping Rule in "exceptional circumstances" only. In reviewing exemptive requests, NASD generally has established high standards and required a firm to establish that it has alternative procedures to assure supervision at a level functionally equivalent to a taping system.

5. Increase Duration of the Special Supervisory Requirements

The amendments extend the time period for which firms must maintain taping systems from two years to three years. The period for which firms are required to maintain the taping system begins from the date that the member establishes its special supervisory procedures and implements the taping system. The amendments further clarify that a firm is required to both establish and implement the taping system within 60 days of receiving notice from NASD or obtaining actual knowledge that it is subject to the Taping Rule.

Publication of the Identity of Firms Subject to the Taping Rule

The amendments allow investors and the general public to ascertain, upon request, whether an identified firm is subject to the Taping Rule. Inquiries about whether a particular firm is subject to the Taping Rule may be made through the Public Disclosure Program's toll-free telephone listing.

Endnotes

- 1 Firms that, as of October 14, 2002, have a pending exemption request from the Taping Rule requirements, based on the firm's first-time triggering of the Rule, (or related appeal before the (National Adjudicatory Council) (NAC)), or for which the time period in which to seek an applicable exemption (or related appeal to the NAC) has not yet expired, may elect to comply with the Taping Rule as modified by the amendments in lieu of complying with the current requirements under the Rule.
- 2 Firms that reduce their staffing levels pursuant to the amendments may consider reporting the termination as a voluntary termination on the Form U-5.

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ATTACHMENT A

New language is underlined; deletions are in brackets.

3010. Supervision

(a) No Change.

(b) Written Procedures

(1) No Change.

(2) Tape recording of conversations

~~(A) [(i)]~~ Each member that either is notified by NASD Regulation or otherwise has actual knowledge that it meets one of the criteria in paragraph (b)(2)(H)~~[(viii)]~~ relating to the employment history of its registered persons at a Disciplined Firm as defined in paragraph (b)(2)~~[(j)]~~~~[(x)]~~ shall establish, maintain, and enforce special written procedures for supervising the telemarketing activities of all of its registered persons.

~~(B) [(ii)]~~ The member must establish and implement the supervisory procedures required by this paragraph within [30] 60 days of receiving notice from NASD Regulation or obtaining actual knowledge that it is subject to the provisions of this paragraph.

A member that meets one of the criteria in paragraph (b)(2)(H) for the first time may reduce its staffing levels to fall below the threshold levels within 30 days after receiving notice from NASD Regulation pursuant to the provisions of paragraph (b)(2)(A) or obtaining actual knowledge that it is subject to the provisions of the paragraph, provided the firm promptly notifies the Department of Member Regulation, NASD Regulation, in writing of its becoming subject to the Rule. Once the member has reduced its staffing levels to fall below the threshold levels, it shall not rehire a person terminated to accomplish the staff reduction for a period of 180 days. On or prior to reducing staffing levels pursuant to this paragraph, a member must provide the Department of Member Regulation, NASD Regulation with written notice, identifying the terminated person(s).

~~(C) [(iii)]~~ The procedures required by this paragraph shall include tape-recording all telephone conversations between the member's registered persons and both existing and potential customers.

(D) [(iv)] The member shall establish reasonable procedures for reviewing the tape recordings made pursuant to the requirements of this paragraph to ensure compliance with applicable securities laws and regulations and applicable rules of [this] the Association. The procedures must be appropriate for the member's business, size, structure, and customers.

(E) [(v)] All tape recordings made pursuant to the requirements of this paragraph shall be retained for a period of not less than three years from the date the tape was created, the first two years in an easily accessible place. Each member shall catalog the retained tapes by registered person and date.

(F) [(vi)] Such procedures shall be maintained for a period of [two] three years from the date that the member establishes and implements the procedures required by the provisions of this paragraph.

(G) [(vii)] By the 30th day of the month following the end of each calendar quarter, each member firm subject to the requirements of this paragraph shall submit to the Association a report on the member's supervision of the telemarketing activities of its registered persons.

(H) [(viii)] The following members shall be required to adopt special supervisory procedures over the telemarketing activities of their registered persons:

- A firm with at least five but fewer than ten registered persons, where 40% or more of its registered persons have been [employed by] associated with one or more Disciplined Firms in a registered capacity within the last three years;
- A firm with at least ten but fewer than twenty registered persons, where four or more of its registered persons have been [employed by] associated with one or more Disciplined Firms in a registered capacity within the last three years;
- A firm with at least twenty registered persons, where 20% or more of its registered persons have been [employed by] associated with one or more Disciplined Firms in a registered capacity within the last three years.

For purposes of the calculations required in subparagraph (H), firms should not include registered persons who:

- (1) have been registered for an aggregate total of 90 days or less with one or more Disciplined Firms within the past three years; and

(2) do not have a disciplinary history.

(I)(ix) For purposes of this Rule, the term "registered person" means any person registered with the Association as a representative, principal, or assistant representative pursuant to the Rule 1020, 1030, 1040, and 1110 Series or pursuant to Municipal Securities Rulemaking Board ("MSRB") Rule G-3.

(J)(x) For purposes of this Rule, the term "disciplined firm" means a member that, in connection with sales practices involving the offer, purchase, or sale of any security, has been expelled from membership or participation in any securities industry self-regulatory organization or is subject to an order of the Securities and Exchange Commission revoking its registration as a broker/dealer.

(K)(xi) For purposes of this Rule, the term "disciplinary history" means a finding of a violation by a registered person in the past five years by the Securities and Exchange Commission, a self-regulatory organization, or a foreign financial regulatory authority of one or more of the provisions (or comparable foreign provision) listed in IM-1011-1 or rules or regulations thereunder.

(L) Pursuant to the Rule 9600 Series, the Association may in exceptional circumstances, taking into consideration all relevant factors, exempt any member unconditionally or on specified terms and conditions from the requirements of this paragraph [upon a satisfactory showing that the member's supervisory procedures ensure compliance with applicable securities laws and regulations and applicable rules of the Association].

* * *

IM-8310-2. Release of Disciplinary [Information] and Other Information Through the Public Disclosure Program

(a) In response to a written inquiry, electronic inquiry, or telephonic inquiry via a toll-free telephone listing, the Association shall release certain information contained in the Central Registration Depository regarding a current or former member, an associated person, or a person who was associated with a member within the preceding two years, through the Public Disclosure Program. Such information shall include:

(1) the person's employment history and other business experience required to be reported on Form U-4;

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- (2) currently approved registrations for the member or associated person;
 - (3) the main office, legal status, and type of business engaged in by the member; and
 - (4) an event or proceeding—
 - (A) required to be reported under Item 23 on Form U-4;
 - (B) required to be reported under Item 11 on Form BD; or
 - (C) reported on Form U-6.

The Association also shall make available through the Public Disclosure Program certain arbitration decisions against a member involving a securities or commodities dispute with a public customer. In addition, the Association shall make available in response to telephonic inquiries via the Public Disclosure Program's toll-free telephone listing whether a particular member is subject to the provisions of Rule 3010(b)(2). The Association shall not release through the Public Disclosure Program social security numbers, residential history information, or physical description information, or information that the Association is otherwise prohibited from releasing under Federal law.

(b) through (l) No Change.

Notice to Members

JULY 2005

GUIDANCE

SUGGESTED ROUTING

Executive Representatives
Legal & Compliance
Senior Management

Taping Rule

SEC Approves Amendments Relating to Taping Rule
"Opt Out" and Exemption Provisions; **Effective Date:
August 1, 2005**

KEY TOPICS

Rule 3010
Taping Rule

Executive Summary

On May 5, 2005, the Securities and Exchange Commission approved amendments to paragraph (l) of Rule 3010(b)(2) (Taping Rule or Rule). The amendments require member firms that are seeking an exemption from the Rule to submit their exemption requests to NASD within 30 days of receiving notice from NASD or obtaining actual knowledge that they are subject to the provisions of the Rule. The amendments also clarify that firms that trigger application of the Taping Rule for the first time can elect to either avail themselves of the one-time "opt out provision" or seek an exemption from the Rule, but they may not seek both options.¹

The Rule, as amended, is set forth in Attachment A. The amendments become effective on August 1, 2005.

Questions/Further Information

Questions concerning this *Notice* may be directed to Afshin Atabaki, Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8902; or Courtney A. Dinsmore, Senior Attorney, Department of Member Regulation, at (202) 728-8402.

Background and Discussion

The Taping Rule, which has been in effect since 1998, is designed to ensure that members with a significant number of registered persons that previously were employed by firms that have been expelled from membership or have had their registrations revoked for sales practice violations (Disciplined Firms) have proper supervisory procedures in place relating to telemarketing activities to prevent fraudulent and improper sales practices or other customer harm.

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NASD/NTV JULY 2005

Under the Rule, member firms that hire a specified number of registered persons from Disciplined Firms must establish, maintain, and enforce special written procedures for supervising the telemarketing activities of all their registered persons. Such procedures must include tape-recording all telephone conversations between such firms' registered persons and both existing and potential customers. The Rule provides firms up to 60 days from the date they receive notice from NASD or obtain actual knowledge that they are subject to the provisions of the Rule to establish and implement the required supervisory procedures, including installing taping systems. Such firms also are required to review the tape recordings, maintain appropriate records, and file quarterly reports with NASD.

The Taping Rule permits member firms that become subject to the Rule for the first time a one-time opportunity to adjust their staffing levels to fall below the prescribed threshold levels and thus avoid application of the Rule (often referred to as the "opt out provision"). A firm that elects this one-time option must reduce its staffing levels to fall below the applicable threshold levels within 30 days after receiving notice from NASD or obtaining actual knowledge that it is subject to the provisions of the Rule. Once a firm has made the reductions, the firm is not permitted to rehire the terminated individuals for at least 180 days.

NASD also has the authority to grant exemptions from the Rule in "exceptional circumstances." In reviewing exemption requests, NASD generally has required a firm to establish that it has alternative procedures to assure supervision at a level functionally equivalent to a taping system. Prior to these amendments to Rule 3010(b)(2)(L), the Rule was silent on the time frame for submitting an exemption request. However, because the Rule provides a firm a total of 60 days from the date it receives notice from NASD or obtains actual knowledge that it is subject to the provisions of the Rule to implement the required supervisory procedures, a firm implicitly has that 60-day period to submit an exemption request.

A firm that submits an exemption request is not required to establish and implement the required supervisory procedures, including the taping system (*i.e.*, such requirements are "tolled") while the staff is reviewing the request and during the course of any subsequent appeals to NASD's National Adjudicatory Council (NAC). NASD tolls the Taping Rule's requirements during the exemption appeal process primarily due to the significant costs involved with installing a taping system and the possibility that the staff or NAC will grant the exemption. At the same time, firms often wait until the 60th day (or shortly before) to request the exemption, which, assuming the exemption was not granted, only further prolonged the establishment and implementation of the required supervisory procedures.

To reduce these possible delays in implementation of the Taping Rule requirements, NASD has amended Rule 3010(b)(2)(L) to require firms that are seeking an exemption from the provisions of the Rule to submit their exemption requests to NASD within 30 days of receiving notice from NASD or obtaining actual knowledge that they are subject to the provisions of the Rule. Specifying a time frame for submitting an exemption request is consistent with the investor protection concerns that the Rule is intended to address, especially given that the requirement to establish and implement the appropriate supervisory procedures is tolled upon the submission of an exemption request. Moreover, based on NASD's experience, 30 days will provide ample time for firms to decide whether to seek an exemption and to submit their requests to NASD.

NASD also received inquiries from some firms as to whether they could elect to use the "opt out" while simultaneously seeking an exemption, with the goal being that the firm would be granted an exemption and be able to immediately rehire the persons whose employment was terminated as part of the "opt out" (rather than waiting the requisite 180 days). However, firms may not pursue these two alternatives simultaneously. A core purpose of the "opt out provision" is to provide relief to those firms that may have inadvertently or unintentionally become subject to the Taping Rule for the first time due, for example, to sudden turnover among registered persons or other events beyond the firm's control. In contrast, exemptions, which are granted only in "exceptional circumstances," are for those situations where the firm has demonstrated that it has supervisory procedures that are equivalent to a taping system or is otherwise in a truly unique situation. It would be inconsistent with the purposes of these two provisions to permit a firm to pursue both options with NASD, either simultaneously or one after the other.

Accordingly, NASD has amended Rule 3010(b)(2)(L) to clarify that firms that trigger application of the Taping Rule for the first time must elect to either avail themselves of the one-time "opt out provision" (i.e., make the staff adjustment to fall below the thresholds of the Rule) or seek an exemption from the Rule, but they may not elect to do both. Pursuant to the amended Rule, firms that become subject to the Taping Rule for the first time have 30 days to decide between the above options.

Endnote

- 1 See Securities Exchange Act Release No. 51658 (May 5, 2005), 70 FR 24848 (May 11, 2005) (Order Granting Approval of Proposed Rule Change Relating to Taping Rule "Opt Out" and Exemption Provisions; File No. SR-NASD-2005-033).

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ATTACHMENT A

New language is underlined; deleted language is in brackets.

3010. Supervision

(a) No Change.

(b) Written Procedures

(1) No Change.

(2) Tape recording of conversations

(A) Each member that either is notified by NASD [Regulation] or otherwise has actual knowledge that it meets one of the criteria in paragraph (b)(2)(H) relating to the employment history of its registered persons at a Disciplined Firm as defined in paragraph (b)(2)(J) shall establish, maintain, and enforce special written procedures for supervising the telemarketing activities of all of its registered persons.

(B) The member must establish and implement the supervisory procedures required by this paragraph within 60 days of receiving notice from NASD [Regulation] or obtaining actual knowledge that it is subject to the provisions of this paragraph.

A member that meets one of the criteria in paragraph (b)(2)(H) for the first time may reduce its staffing levels to fall below the threshold levels within 30 days after receiving notice from NASD [Regulation] pursuant to the provisions of paragraph (b)(2)(A) or obtaining actual knowledge that it is subject to the provisions of the paragraph, provided the firm promptly notifies the Department of Member Regulation, NASD [Regulation], in writing of its becoming subject to the Rule. Once the member has reduced its staffing levels to fall below the threshold levels, it shall not rehire a person terminated to accomplish the staff reduction for a period of 180 days. On or prior to reducing staffing levels pursuant to this paragraph, a member must provide the Department of Member Regulation, NASD [Regulation] with written notice, identifying the terminated person(s).

(C) No Change.

(D) The member shall establish reasonable procedures for reviewing the tape recordings made pursuant to the requirements of this paragraph to ensure compliance with applicable securities laws and regulations and applicable rules of [the Association] NASD. The procedures must be appropriate for the member's business, size, structure, and customers.

(E) through (F) No Change.

(G) By the 30th day of the month following the end of each calendar quarter, each member firm subject to the requirements of this paragraph shall submit to [the Association] NASD a report on the member's supervision of the telemarketing activities of its registered persons.

(H) No Change.

(I) For purposes of this Rule, the term "registered person" means any person registered with [the Association] NASD as a representative, principal, or assistant representative pursuant to the Rule 1020, 1030, 1040, and 1110 Series or pursuant to Municipal Securities Rulemaking Board ("MSRB") Rule G-3.

(J) through (K) No Change.

(L) Pursuant to the Rule 9600 Series, [the Association] NASD may in exceptional circumstances, taking into consideration all relevant factors, exempt any member unconditionally or on specified terms and conditions from the requirements of this paragraph. A member seeking an exemption must file a written application pursuant to the Rule 9600 Series within 30 days after receiving notice from NASD or obtaining actual knowledge that it meets one of the criteria in paragraph (b)(2)(H). A member that meets one of the criteria in paragraph (b)(2)(H) for the first time may elect to reduce its staffing levels pursuant to the provisions of paragraph (b)(2)(B) or, alternatively, to seek an exemption pursuant to paragraph (b)(2)(L), as appropriate; such a member may not seek relief from the Rule by both reducing its staffing levels pursuant to paragraph (b)(2)(B) and requesting an exemption.

(3) through (4) No Change.

(c) through (g) No Change.

NASD Notice to Members 98-52

SEC Approves Taping Rule; Effective August 17, 1998

Suggested Routing

- Senior Management
- Advertising
- Continuing Education
- Corporate Finance
- Executive Representatives
- Government Securities
- Institutional
- Insurance
- Internal Audit
- Legal & Compliance
- Municipal
- Mutual Fund
- Operations
- Options
- Registered Representatives
- Registration
- Research
- Syndicate
- Systems
- Trading
- Training
- Variable Contracts

Executive Summary

On April 17, 1998, in Release No. 34-39883, the Securities and Exchange Commission (SEC) approved an amendment to National Association of Securities Dealers, Inc. (NASD[®]) Rule 3010 to require members to establish special supervisory procedures, including the tape recording of conversations, when they have hired more than a specified percentage of registered persons from certain firms that have been expelled or that have had their broker/dealer registrations revoked for violations of sales practice rules (the Taping Rule or Rule).¹ The new Rule will be effective on August 17, 1998. The text of the new Rule and the *Federal Register* version of the SEC release are attached.

Interpretive questions concerning the new Rule should be directed to Mary Revell, Associate General Counsel, NASD Regulation, Inc., at (202) 728-8203. Questions concerning compliance with the new Rule should be directed to Susan Lang, Senior Research Analyst, Department of Member Regulation, NASD RegulationSM, at (202) 728-6969. Members should submit reports required by the Taping Rule to Compliance, Department of Member Regulation, NASD Regulation, 1735 K Street, N.W., Washington, D.C. 20006.

Background

The Taping Rule was developed to respond to two issues. First, it responds to concerns expressed in the *Joint Regulatory Sales Practice Sweep (Sweep) Report*² regarding the need for heightened supervision of certain registered representatives with troubled regulatory and compliance records. The Rule also addresses the particular problems that occur when a firm hires a large number of individuals who formerly worked at a firm that has been expelled or has had its registration

revoked and where they were inadequately supervised and trained.

The NASD initially published the Taping Rule for comment in *Notice to Members 96-59*. NASD Regulation revised the proposal in response to the 42 comment letters that were received, and filed the proposed Taping Rule with the SEC for approval in September 1997.

The SEC published notice of the proposed Taping Rule and one amendment to the Rule in the *Federal Register* in December 1997. The SEC received one comment letter on the proposed Rule. The SEC approved the proposed Rule, as amended, and Amendment No. 2 to the proposed Rule on April 17, 1998.

The text of the new Taping Rule is set forth below. For a complete description of the history of the Rule, members should review in detail the attached *Federal Register* version of the SEC release.

Taping Rule

The Taping Rule will apply whenever a specified percentage of a member firm's sales force is comprised of registered persons who were employed within the last three years by a firm that has been expelled from membership in a securities industry self-regulatory organization or has had its registration as a broker/dealer revoked by the SEC (a Disciplined Firm). The requisite percentage varies depending on the size of the firm, from 40 percent for a small firm to 20 percent for a larger firm. The firm must establish the required supervisory procedures within 30 days of receiving notice from NASD Regulation, or obtaining actual knowledge, that it is subject to the provisions of the Rule.

Under the Taping Rule, if the requisite percentage of a member's sales

force previously was employed by a Disciplined Firm, the member will be required to adopt special written procedures to supervise the telemarketing activities of all of its registered persons. The procedures require, at a minimum, that the member tape record all telephone conversations between all of its registered persons and both existing and potential customers for a period of two years. The measures required by the Rule are designed to prevent a reoccurrence of sales practice abuse or other customer harm that caused the Disciplined Firm to be expelled or have its registration revoked.

The Rule requires that firms ensure that they tape record any means of telecommunications that is regularly used by registered persons to communicate with customers. In connection with this requirement, firms should ensure that the means of telecommunications used is capable of being taped. If, for example, registered persons use cellular phones on a regular basis to call customers, and it is not possible to tape record cellular telephone conversations, a firm should prohibit the use of cellular telephones for communicating with customers. On the other hand, the occasional use of a cellular telephone where warranted for other business reasons would not be prohibited.

The Rule also requires firms subject to the taping requirement to establish reasonable procedures for reviewing tape recordings to ensure compliance with securities laws and NASD rules, to submit reports to the NASD on their supervision of telemarketing, and to retain and catalog the tapes. NASD Regulation believes that, in adopting review procedures reasonably designed to comply with this requirement, members generally would be expected to:

- specify the minimum percentage of

tape recordings that must be reviewed and how the review will be conducted, or, if a random review is utilized, specify how the random review will be conducted;

- identify one or more senior persons at the firm with appropriate knowledge and training to review the tape recordings;
- identify how the supervisory review will be conducted and documented;
- consider the complaint and overall disciplinary history, if any, of registered persons whose telephone conversations are being recorded in establishing the review procedures and specifying the minimum percentage of tape recordings that must be reviewed (with particular emphasis on complaints regarding telemarketing);
- maintain records documenting how and when tape recordings are reviewed; and
- monitor to ensure that the procedures are being implemented and complied with.

The factors above are not exclusive and members must consider all appropriate factors when developing their review procedures and implementing their supervisory reviews.

In complying with the Taping Rule, members must comply with federal and state civil and criminal statutes governing the tape recording of conversations. Each state has a statute governing wiretapping; there also is a federal statute governing wiretapping and electronic surveillance.³ The federal statute and the majority of the state statutes permit taping of telephone conversations with the consent of one party (one-party statutes);⁴ a minority of state statutes require the consent of all parties to the conversation (two-party

statutes).⁵ Three issues arise from the proposed Rule: what is necessary to comply with one-party statutes; what is necessary to comply with two-party statutes; and how to comply where a conversation occurs between a person in a one-party state and a person in a two-party state.

The question of which state law applies when a conversation occurs between a person in a one-party statute state and a person in a two-party statute state is an open issue that depends on the individual laws of each state and the individual facts. Firms would be required to independently determine that state laws are satisfied. The best practice in each case would be for member firms to notify their registered persons and customers that their telephone calls are being tape recorded.

While each firm is responsible for complying with the Taping Rule, NASD Regulation will provide firms with all of the information they need to determine if they are subject to the requirements of the Rule. NASD Regulation will make a monthly determination of which firms are subject to the Rule. NASD Regulation will then notify each firm that is subject to the Rule and that it has 30 days to establish the supervisory procedures required by the Rule. NASD Regulation also will compile and maintain a list of firms that met the definition of "Disciplined Firm" within the last three years that will be placed on the NASD Regulation Web Site (www.nasdr.com). A copy of the initial list is attached to this Notice.

NASD Regulation believes that firms should be able to rely on the accuracy of the information provided to them. Firms that are notified by NASD Regulation that they are subject to the Rule must establish the procedures required by the Rule. Firms that do not receive this noti-

cation are not required to establish the special supervisory procedures. However, if a firm has actual knowledge, inconsistent with the information relied upon by NASD Regulation, that it is subject to the Rule, NASD Regulation anticipates that the firm will be disciplined for failure to comply with the Rule.

Finally, any member required to adopt these procedures may seek an exemption from the requirement. NASD Regulation may grant an exemption upon a satisfactory showing that the member's supervisory procedures ensure compliance with applicable securities laws and regulations and NASD rules. Members should follow the procedures detailed in the Rule 9600 Series when seeking an exemption.

this paragraph within 30 days of receiving notice from NASD Regulation or obtaining actual knowledge that it is subject to the provisions of this paragraph.

(iii) The procedures required by this paragraph shall include tape-recording all telephone conversations between the member's registered persons and both existing and potential customers.

(iv) The member shall establish reasonable procedures for reviewing the tape recordings made pursuant to the requirements of this paragraph to ensure compliance with applicable securities laws and regulations and applicable rules of this Association. The procedures must be appropriate for the member's business, size, structure, and customers.

(v) All tape recordings made pursuant to the requirements of this paragraph shall be retained for a period of not less than three years from the date the tape was created, the first two years in an easily accessible place. Each member shall catalog the retained tapes by registered person and date.

(vi) Such procedures shall be maintained for a period of two years from the date that the member establishes the procedures required by the provisions of this paragraph.

(vii) By the 30th day of the month following the end of each calendar quarter, each member firm subject to the requirements of this paragraph shall submit to the Association a report on the member's supervision of the telemarketing activities of its registered persons.

(viii) The following members shall be required to adopt special supervisory procedures over the telemarketing activities of their registered persons:

• A firm with at least five but fewer than ten registered persons, where 40% or more of its registered persons have been employed by one or more Disciplined Firms within the last three years;

• A firm with at least ten but fewer than twenty registered persons, where four or more of its registered persons have been employed by one or more Disciplined Firms within the last three years;

• A firm with at least twenty registered persons, where 20% or more of its registered persons have been employed by one or more Disciplined Firms within the last three years.

(ix) For purposes of this Rule, the term "registered person" means any person registered with the Association as a representative, principal, or assistant representative pursuant to the Rule 1020, 1030, 1040, and 1110 Series or pursuant to Municipal Securities Rulemaking Board ("MSRB") Rule G-3.

(x) For purposes of this Rule, the term "disciplined firm" means a member that, in connection with sales practices involving the offer, purchase, or sale of any security, has been expelled from membership or participation in any securities industry self-regulatory organization or is subject to an order of the Securities and Exchange Commission revoking its registration as a broker/dealer.

(xi) Pursuant to the Rule 9600 Series, the Association may exempt any member unconditionally or on specified terms and conditions from the requirements of this paragraph upon a satisfactory showing that the member's supervisory procedures ensure compliance with applicable securities laws and regulations and applicable rules of the Association.

Text Of Amendments To Rule 3010

(Note: New language is underlined; deletions are bracketed.)

Rule 3010. Supervision

(a) No change

(b) Written Procedures

(1) No change

(2) Tape recording of conversations

(i) Each member that either is notified by NASD Regulation or otherwise has actual knowledge that it meets one of the criteria in paragraph (b)(2)(viii) relating to the employment history of its registered persons at a Disciplined Firm as defined in paragraph (b)(2)(x) shall establish, maintain, and enforce special written procedures for supervising the telemarketing activities of all of its registered persons.

(ii) The member must establish the supervisory procedures required by

(3)(2) No change to text

(4)(3) No change to text

(c) through (g) No change

Text Of Amendments To Rule 9610

(Note: New language is underlined.)

Rule 9600. Procedures for Exemptions

Rule 9610. Application

(a) File With General Counsel

A member seeking an exemption from Rule 1021, 1022, 1070, 2210, 2340, 2520, 2710, 2720, 2810, 2850, 2851, 2860. Interpretive Material 2860-1, 3010(b)(2), 3350, 11870, or 11900, Interpretive Material 2110-1, or Rule G-37 shall file a written application with the appropriate department or staff of the Association and provide a copy of the application to the Office of General Counsel of NASD Regulation.

Disciplined Firms⁶

- A. R. Baron & Co., Inc.
- Banc Street Securities, Inc.
- Beacon Securities, Inc.
- Capital Investment Managers, Inc.
- Coastline Financial, Inc.
- Escalator Securities, Inc.
- Euro-Atlantic Securities Inc.
- F.N. Wolf & Co., Inc.
- Feltman & Co.
- H. L. Camp & Company, Inc.

- Hibbard Brown & Co., Inc.
- Jaron Equities Corp.
- Johnston Kent Securities, Inc.
- Kinlaw Securities Corporation
- L. C. Wegard & Co., Inc.
- M. H. Novick & Co., Inc.
- M. Rimson & Co., Inc.
- M.G.S.I. Securities, Inc.
- Penn Capital Financial Services, Inc.
- Prime Investors, Inc.
- Retirement Investment Group
- Selheimer & Co.
- Shaner & Company, Inc.
- Stratton Oakmont Inc.
- Townsend Associates & Company, Inc.
- U.S. Securities Corporation of Washington, D.C.
- Westcap Securities, L.P.

Endnotes

¹ 63 FR 20232 (April 23, 1998). See also correction in Release No. 34-39883A (April 23, 1998), 63 FR 24202 (May 1, 1998).

² Staffs of the NASD, New York Stock Exchange (NYSE), North American Securities Administrators Association (NASAA), and the Office of Compliance Inspections and Examinations, SEC, *Joint Regulatory Sales Practice Sweep: A Review of the Sales Practice Activities of Selected Registered Representatives and the Hiring, Retention, and Supervisory Practices of the Brokerage Firms Employing Them* (March 1996). The Sweep was an initiative involving the staffs of the NASD, the SEC, the NYSE, and representatives of NASAA to review the sales practice activities of selected registered representatives and the hiring, retention, and supervisory practices of the brokerage firms employing them in order to

identify possible problem registered representatives, review their sales practices, and assess whether adequate hiring, retention, and supervisory mechanisms were in place. The *Sweep Report* was released on March 18, 1996.

³ 18 U.S.C. § 2519 *et seq.*

⁴ In one-party statute states, the only issue is whether the registered person knows of and consents to the tape recording. The recording requirement would run to the firm, and the equipment would be the firm's. Therefore, it would be necessary for the firm to ensure that the person has notice and consents to the tape recording of his or her telephone conversations. This could be accomplished through a clause in an employment agreement or employee handbook or other written notice to the registered person.

⁵ In two-party statute states, it would be necessary to insert on the firm's telephone line a recording stating that all telephone conversations are being taped, similar to customer service lines in other industries. Some states require a system of beeps or buzzers that sound throughout the conversation. Some states also have a "business use exception" to the two-party statute consent requirement, but it is worded and applied differently in each state.

⁶ This list is comprised of firms that were disciplined within the last three years and was compiled based on information available as of June 15, 1998.

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however, if more than six years have elapsed from the transaction, occurrence, or event giving rise to the claim, under Rule 10304 of the Code, the claim will not be eligible for submission to arbitration.¹¹ All claims involving general securities broker/dealers will continue to be accepted for arbitration consistent with past practice. Claims previously submitted that the Office has already declined to arbitrate under the old policy cannot be resubmitted under the policy being announced herein.

2. Statutory Basis

NASD Regulation believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act¹² in that eliminating a barrier to the arbitration of disputes involving exempted securities, public customers and members will have access to a fair, efficient, and cost-effective forum for the resolution of such disputes.

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

The NASD does not believe that the proposed rule change will impose any inappropriate burden on competition.

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

No written comments were either solicited or received.

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

Within 35 days of the publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve the proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing,

¹¹ NASD Regulation notes that it has a proposed amendment to Rule 10304, rule filing SR-NASD-97-44, pending approval with the SEC. Under the proposed rule change all claims are presumed to be eligible; however, the presumption can be overcome if the respondent challenges the claim on the basis that more than six years have elapsed since the act or occurrence giving rise to the claim.

¹² 15 U.S.C. 78-3.

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, N.W., Washington, D.C. 20549. 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 at 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-98-04 and should be submitted by May 14, 1998.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹³

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 98-10754 Filed 4-22-98; 8:45 am]

BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39883; File No. SR-NASD-97-69]

Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change, as Amended, and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 2 to the Proposed Rule Change by the National Association of Securities Dealers, Inc. Relating to the Tape Recording of Conversations

April 17, 1998.

I. Introduction

On September 12, 1997, the National Association of Securities Dealers, Inc. ("NASD"), through its regulatory subsidiary NASD Regulation, Inc. ("NASD Regulation") filed with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),¹ and Rule 19b-4 thereunder.² In this filing, NASD Regulation proposed amendments to Rule 3010 to

require the tape recording of conversations where members hire more than a specified percentage of registered persons from certain firms that have been expelled or that have had their broker/dealer registration revoked for violations of sales practices rules. The proposed rule change also includes a conforming rule change to Rule 9610. Notice of this proposed rule change was published in the Federal Register on December 5, 1997 (as amended, the "Notice").³ The Commission received one comment letter, which expressed concerns about using tape recording as a method of supervision, in response to the Notice.⁴ On March 9, 1998, NASD Regulation filed Amendment No. 2 with the Commission.⁵ This order approves the rule change, as amended, and grants accelerated approval of Amendment No. 2 to the rule change.

II. Background

At its meeting in July 1996, the NASD Regulation Board of Directors authorized the staff to issue a Notice to Members soliciting comment on proposed changes to NASD supervisory Rule 3010 to require the tape recording of telephone conversations of registered representatives in certain circumstances. The Rule was developed both to respond to concerns expressed in the *Joint Regulatory Sales Practice Sweep ("Sweep") Report*⁶ regarding the

³ See Securities Exchange Act Release No. 39361 (November 26, 1997), 62 FR 64422 (File No. SR-NASD-97-69), Amendment No. 1 to the proposed rule filing was filed on November 12, 1997. The changes contained in this amendment were included in the Notice. See Letter from Mary N. Revell, Associate General Counsel, NASD Regulation, to Katherine A. England, Assistant Director, Division of Market Regulation, Commission (November 17, 1997).

⁴ See Letter from R. Gerald Baker, Securities Industry Association ("SIA"), to Jonathan C. Katz, Secretary, Commission, dated February 11, 1998.

⁵ See letter from Mary N. Revell, Associate General Counsel, NASD Regulation, to Katherine A. England, Assistant Director, Office of Market Supervision, Division of Market Regulation (March 9, 1998). In Amendment No. 2, NASD Regulation: (1) Applies the proposal to firms that have a work force comprised of a specified number of registered persons who were employed by a "disciplined firm" within the last three years instead of two years; (2) requires firms to establish special procedures to supervise the telemarketing activities of registered persons instead of registered representatives; (3) amends the definition of registered persons to include those persons who register as municipal securities principals or representatives pursuant to Municipal Securities Rulemaking Board Rule G-3; and (4) provides guidance on what would constitute "reasonable procedures for reviewing the tape recordings made pursuant to the requirements of" the taping rule in a Notice to Members announcing approval of the rule.

⁶ Staffs of the NASD, New York Stock Exchange ("NYSE"), North American Securities Administrators Association ("NASAA"), and the Office of Compliance Inspections and

¹³ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

need for heightened supervision of certain registered representatives with troubled regulatory and compliance records and also to address the particular problems that occur when a firm hires a larger number of individuals who formerly worked at a firm that has been expelled or has had its registration revoked (a "Disciplined Firm") where they were inadequately supervised and trained.

NASD Regulation stated in its filing that one of the key findings of the Sweep Report concerned the willingness of some firms to employ registered representatives with a history of disciplinary actions or customer complaints.⁷ Based on this finding, the Working Group collectively recommended that firms that hire registered representatives with a recent disciplinary history involving sales practice abuse or other customer harm should implement special supervisory procedures tailored to the individual registered representative, which include a heightened level of scrutiny of the registered representative's activities by his or her supervisor, for a period of time.⁸ The Sweep Report recommended that, if firms fail to establish such special supervisory procedures, the self-regulatory organizations ("SROs") should consider revising their rules to specifically require that registered representatives with a recent history of disciplinary actions involving sales practice abuse or other customer harm be placed under special supervision by the firm for a period of time.

NASD Regulation and the NYSE have issued a memorandum discussing the Sweep Report and providing guidance on actions firms could take to provide heightened supervision of problem registered representatives.⁹ While the special procedures designed to provide a heightened level of supervision recommended by the Sweep Report and described in the NASD/NYSE

Examinations, SEC, *Joint Regulatory Sales Practice Sweep: A Review of the Sales Practice Activities of Selected Registered Representatives and the Hiring, Retention, and Supervisory Practices of the Brokerage Firms Employing Them* (March 1996). The Sweep was an initiative involving the staffs of the NASD, the SEC, the NYSE, and representatives of the NASAA (collectively, the "Working Group") to review the sales practice activities of selected registered representatives and the hiring, retention, and supervisory practices of the brokerage firms employing them in order to identify possible problem registered representatives, review their sales practices, and assess whether adequate hiring, retention, and supervisory mechanisms are in place. The Sweep Report was released on March 18, 1996.

⁷ The current proposal focuses on the disciplinary history of the firm that formerly employed the registered representative.

⁸ *Id.* at II, iv.

⁹ NASD Notice of Members 97-19 (April 1997); NYSE Information Memo 97-20 (April 15, 1997).

memorandum may provide adequate supervision of associated persons in most circumstances, NASD Regulation proposes to adopt specific procedures in certain situations in order to provide the level of supervision required by Rule 3010.

NASD Regulation proposes to amend NASD Rule 3010 to require firms that hire a specified number of individuals from Disciplined Firms to tape-record telephone conversations between their registered persons and existing and potential customers. The proposed Rule would apply when a firm hires a substantial number of registered persons from a firm or firms that have been expelled or had their registrations revoked for sales practice abuse. The measures are designed to prevent a reoccurrence of sales practice abuse or other customer harm that caused the Disciplined Firm to be expelled or have its registration revoked. The proposal is similar to an interpretation adopted by the National Futures Association ("NFA") in 1993 to combat abusive cold calling.¹⁰ The NFA's interpretation is discussed below.

A. Notice to Members 96-59 and Original Proposal

In its filing with the Commission, NASD Regulation described Notice to Members 96-59 ("NTM 96-59"), which contained the original proposed Rule ("original proposal" or "original Rule").¹¹ NASD Regulation's original proposal captured a broader swath of firms. It would have been triggered whenever a significant portion of a member's work force was comprised of associated persons who formerly were employed by a Disciplined Firm or firms or when the firm itself was a Disciplined Firm. The original proposal defined a Disciplined Firm, for purposes of the Rule, as one that had been disciplined (e.g., expelled, suspended, or enjoined) by a regulatory entity, an SRO, or a court within the previous five years for telemarketing or sales-practice abuses in connection with the solicitation, offer, or sale of securities.

NASD Regulation's original proposal also stated that if more than 20 percent of a member's sales force of associated persons previously were employed by a Disciplined Firm, the member would have been required to adopt special written procedures to supervise the telemarketing activities of its associated persons. Firms that were themselves

¹⁰ See Letter from Lynn K. Gilbert, Deputy Director, Commodity Futures Trading Commission, to Daniel J. Roth, General Counsel, NFA (January 19, 1993).

¹¹ See Notice to Members 96-59 (September 1996).

Disciplined Firms also would have been required to adopt these procedures. The procedures would have required, at a minimum, that the employer member tape record all telephone conversations between all of its associated persons and both existing and potential customers, and maintain these procedures for two years. For each firm that was itself a Disciplined Firm, at the end of the two-year period, NASD Regulation would have conducted an evaluation to determine whether, and for how long, the firm would continue to be subject to the requirements of the Rule. The Rule also would have required firms subject to the taping requirement to review the tapes periodically to ensure compliance with securities laws and NASD rules, to submit reports to NASD Regulation on their supervision of telemarketing activities, and to retain and index the tapes.

B. Comments and Response on the Original Proposal

NASD Regulation received 42 comment letters in response to its initial Notice to Members.¹² Of the 42

¹² NASD Regulation received the following comment letters: (1) Letter from Brian C. Underwood, A.G. Edwards & Sons, Inc. ("Edwards"), dated October 31, 1996; (2) Letter from Kevin P. Howe, American Express Financial Advisors ("AEFA"), dated October 31, 1996; (3) Letter from G. Thomas Mitchell, Aurora Insurance and Securities, Inc. ("Aurora"), dated October 10, 1996; (4) Letter from Jerome Snyder, Burlington Capital Group, L.P. ("Burlington"), dated October 23, 1996; (5) Letter from Leslie D. Smith, Berthel Fisher Company ("Berthel"), dated October 25, 1996; (6) Letter from Walter I. Miller, Capital Growth Planning, Inc. ("Capital"), dated September 24, 1996; (7) Letter from Sanford D. Greenberg, Chatfield Dean & Co. ("Chatfield Dean"), dated October 31, 1996; (8) Letter from Neil Lawrence Lane, Citicorp Investment Services ("CIS"), dated October 31, 1996; (9) Letter from David J. Master, Coastal Securities ("Coastal"), dated October 31, 1996; (10) Letter from John Polanin, Jr., Cowen & Company ("Cowen"), dated November 7, 1996; (11) Letter from Richard L. Sandow, Cullum & Sandow Securities, Inc. ("Cullum"), dated October 17, 1996; (12) Letter from Gregg Thaler, Duke & Company, Inc. ("Duke I"), dated October 10, 1996; (13) Letter from William Rotholz, Duke & Company, Inc. ("Duke II"), dated October 29, 1996; (14) Letter from Shannon Braymen, Duncan-Smith Securities, Inc. ("Duncan-Smith"), dated October 22, 1996; (15) Letter from James H. Pyle et al., E.E. Powell & Company, Inc., dated October 21, 1996; (16) Letter from Nancy K. Port, Equity Services, Inc. ("EST"), dated October 30, 1996; (17) Letter from Rick Fetterman, Fetterman Investments, Inc., dated October 1, 1996; (18) Letter from Herbert O. Sontz, GKN Securities ("GKN"), dated October 31, 1996; (19) Letter from Lawrence E. Wesneski, Hoak Breedlove Wesneski & Co. ("Hoak"), dated October 21, 1996; (20) Letter from Cabell B. Birdsong, Investors Security Company, Inc. ("ISC"), dated October 22, 1996; (21) Letter from David A. Rich, Jefferies & Company, Inc., dated November 8, 1996; (22) Letter from Thomas P. Kourtris, John Hancock Distributors, Inc., dated September 23, 1996; (23) Letter from A.E. Monahan, Keystone Capital Corporation ("Keystone"), dated October 7, 1996;

Continued

comment letters. 39 were opposed to the proposal, including those filed by the Securities Industry Association, Lehman Brothers, Merrill Lynch, Morgan Stanley, and Smith Barney. NASD Regulation stated that most of the commenters supported the NASD's objective in proposing the taping Rule and agreed that firms should be discouraged from recruiting groups of registered persons from a Disciplined Firm, however, they did not believe that tape recording of conversations was an appropriate regulatory requirement and feared that regulators will require even more comprehensive tape recording in the future.

The definition of a Disciplined Firm is too broad: NASD Regulation stated that many of the commenters believe the definition of a Disciplined Firm in the original Rule was too broad. For example, the original definition would have included a firm that was the subject of an injunction for a technical or inadvertent violation of state law or as the result of a consensual injunction involving only a fraction of the firm's business and employees. NASD Regulation responded by narrowing the definition of a Disciplined Firm to include firms that have been expelled from membership in a securities industry SRO or that have had their

(24) Letter from Paul B. Uhlenhop, Lawrence, Kamin, Saunders & Uhlenhop ("Lawrence, Kamin"), dated October 29, 1996; (25) Letter from Kathryn S. Reimann, Lehman Brothers Inc. ("Lehman"), dated October 31, 1996; (26) Letter from Kenneth S. Splrer, Merrill Lynch, Pierce, Fenner & Smith ("Merrill Lynch"), dated November 14, 1996; (27) Letter from Jack G. Levin, Montgomery Securities ("Montgomery"), dated January 16, 1997; (28) Letter from Frederick W. Bogdan, Morgan Stanley & Co., Incorporated ("Morgan Stanley"), dated October 30, 1996; (29) Letter from Dennis S. Kaminski, Mutual Service Corporation ("MSC"), dated October 29, 1996; (30) Letter from Richard Berenger, Nathan & Lewis Securities, Inc. ("Nathan & Lewis"), dated October 18, 1996; (31) Letter from Douglas L. Dunahay, Neldiger/Tucker/Bruner Inc. ("Neldiger"), dated October 29, 1996; (32) Letter from Edward T. Borer, Philadelphia Corporation ("PC"), dated October 17, 1996; (33) Letter from Michael Flannigan, Protective Group Securities Corporation ("PGSC"), dated September 24, 1996; (34) Letter from Robert A. Fitzer, Jr., RAF Financial Corporation ("RAF"), dated October 29, 1996; (35) Letter from Glen F. Hackmann, Robert W. Baird & Co., Incorporated ("Baird"), dated October 31, 1996; (36) Letter from Douglas F. Schofield, Schofield Investments, Inc., dated September 18, 1996; (37) Letter from Richard O. Scribner, Allen B. Holeman, and C. Evan Steward, SIA, dated November 4, 1996; (38) Letter from Dov S. Schechter, Smith Barney Inc. ("Smith Barney"), dated October 31, 1996; (39) Letter from Patrick G. Haayes, Stratton Oakmont, Inc. ("Stratton"), dated October 30, 1996; (40) Letter from Walter H. Schlobohm, dated February 10, 1997; (41) Letter from John Maceranka, The Windmill Group, Inc., dated September 28, 1996; and (42) Letter from Stanley J. Allen Jr., Yee, Desmond, Schroeder & Allen, Inc. ("Yee"), dated October 28, 1996.

registration revoked by the SEC due to telemarketing or sales practice abuses.

The Rule is too broad with respect to the individuals included in the percentage calculation and the time frame: NASD Regulation stated that commenters complained the Rule was too broad in several respects. First, commenters said the Rule would target firms and individuals for the actions of other firms and individuals of which they had no knowledge or control.¹³ Second, the commenters criticized the Rule's application to all individuals that had ever been employed by a Disciplined Firm in the calculation of the percentage that would trigger the special supervisor procedures.¹⁴ Finally, NASD Regulation stated that commenters believed the Rule should be limited to personnel who have contact with customers, such as registered representatives, and should exclude clerical and ministerial employees from both the 20% calculation and the taping requirement.¹⁵

In response, NASD Regulation narrowed the scope of the original Rule to apply only to firms that hire a specified percentage of individuals who were employed at a Disciplined Firm within the last three years. NASD Regulation also limited the individuals calculated in the percentage to register persons, leaving out clerical and ministerial personnel. Also, NASD Regulation limited the persons subject to the taping requirement to registered representative in conversations with both existing and potential customers.

The Rule does not achieve the stated purpose: NASD Regulation noted that several commenters questioned whether the original Rule goes beyond the scope of the Sweep Report and would be effective in achieving the Sweep Report recommendations because taping is not an effective means of supervising sales efforts.¹⁶

NASD Regulation responded by emphasizing that the taping requirement is being restricted to particularly egregious situations. They stated their concern that when a firm hires high percentages of employees from firms that have been expelled by an SRO or that have had their registration revoked by the Commission, these groups of employees are unlikely to have been trained or supervised adequately. In

¹³ See, e.g., letters from Lehman and Morgan Stanley.

¹⁴ See, e.g., letters from Edwards, Morgan Stanley, Nathan & Lewis, PC, SIA, and Stratton.

¹⁵ See, e.g., letters from Edwards, Barington, Chatfield Dean, Cullum, Duke II, ESI, ISC, Morgan Stanley, Baird, and Stratton.

¹⁶ See, e.g., letters from CIS, Duke II, ESI, Lehman, Merrill Lynch, MSC, Nathan & Lewis, and SIA.

addition, NASD Regulation stated its belief in the *In terrorem* effect of recording telephone conversations to deter sales practice abuses. Finally, the NASD believes the Rule directly addresses the issues raised when a firm hires a high percentage of individuals who were employed by a Disciplined Firm where they were inadequately trained and supervised.

The costs of the Rule are too great: The NASD noted that some commenters expressed concerns that the costs of the original Rule would be too high, considering the limited benefits of the Rule. The commenters also stated that the Rule would have a disproportionate effect on small firms.¹⁷

The NASD stated that its narrowing of many aspects of the Rule would result in lower compliance costs. Specifically, in the revised proposal, the NASD exempted firms with five or fewer registered persons from the Rule and tiered the structure for determining the percentage of employees that trigger the taping requirement so that smaller firms would have to hire 30% or more of their registered persons from Disciplined Firms before they would trigger the requirement. In addition, the NASD stated that by narrowing the definition of a Disciplined Firm, fewer firms will be subject to the taping requirement.¹⁸ Finally, with respect to certain practical compliance difficulties, the NASD agreed to provide firms with all the relevant information they need to determine whether they are in compliance with the Rule.

Privacy concerns: The NASD stated that many commenters felt the original Rule would invade the privacy of both a firm's customers as well as the firm's registered representatives, which would be unfair to both firms and registered representatives that did not have disciplinary histories. Commenters also believe that the Rule would conflict with federal and state wiretapping laws. Finally, they are concerned that the

¹⁷ The commenters stated that small firms would be disproportionately effected both in the cost of taping and in the numbers of firms likely to become subject to the threshold percentage of 20%. See letters from Capital, Cowen, Duncan-Smith, Hoak, SIA, and Yee.

¹⁸ The NASD revised the definition of Disciplined Firm to include only expelled and revoked firms in order to focus, at least initially, on the most egregious cases with the greatest supervisory and disciplinary problems. For the two-year period 1995-1996, 14 firms met the definition of Disciplined Firm: 4 firms were expelled from SRO membership and 10 had their registrations revoked. This approach is similar to the one taken by the NFA, and will allow the NASD to gain experience with the implementation of the Rule before it considers expanding the definition of Disciplined Firm to include firms that have been suspended from SRO membership or from SEC registration.

Rule does not restrict the accessibility and manner in which the tapes may be used.¹⁹

As stated above, because the Rule has been revised to address only the most egregious situations, the impact on privacy will be minimized. Also, upon approval, NASD Regulation will inform NASD members that, in complying with this Rule, they must also comply with federal and state civil and criminal statutes governing the tape recording of conversations. This is the same approach the NFA has taken with respect to this issue.²⁰

Each state has a statute governing wiretapping; there also is a federal statute governing wiretapping and electronic surveillance.²¹ The federal statute and the majority of the state statutes permit taping of telephone conversations with the consent of one party ("one-party statutes"),²² a minority of state statutes require the consent of all parties to the conversation ("two-party statutes").²³ Three issues arise from the proposed Rule: what is necessary to comply with one-party statutes; what is necessary to comply with two-party statutes; and how to comply where a conversation occurs between a person in a one-party state and a person in a two-party state. The NASD has left compliance with the state statutes on wiretapping and privacy for each broker-dealer.

C. Proposed Rule

As revised and filed with the Commission, the proposed Rule would apply whenever a specified percentage of a member firm's sales force is

comprised of registered persons who were employed within the last three years by a firm that has been expelled from membership in a securities industry SRO or has had its registration as a broker/dealer revoked by the SEC. The requisite percentage varies depending on the size of the firm, from 40 percent for a small firm to 20 percent for a larger firm. The firm must establish the required supervisory procedures within 30 days of receiving notice from NASD Regulation or obtaining actual knowledge that it is subject to the provisions of the Rule.

Under the proposed Rule, if the requisite percentage of a member's sales force previously was employed by a Disciplined Firm, the member would be required to adopt special written procedures to supervise the telemarketing activities of all of its registered persons. The procedures would require, at a minimum, that the member tape record all telephone conversations between all of its registered persons and both existing and potential customers for a period of three years, and maintain these supervisory procedures for two years. The Rule

would require firms to ensure that they tape record all regularly used means of telecommunications, including cellular phones. The Rule also would require firms subject to the taping requirement to establish reasonable procedures for reviewing the tape recordings to ensure compliance with securities laws and NASD rules, to submit reports to the NASD on their supervision of telemarketing, and to retain and catalog the tapes.

While each firm is responsible for complying with the Rule, NASD Regulation will provide firms with all of the information that they need to determine if they are subject to the requirements of the Rule. NASD Regulation believes that firms should be able to rely on the accuracy of the information provided to them by the NASD. Therefore, the NASD anticipates that a firm will be disciplined for failure to comply with the Rule only if it has actual knowledge of information that would make the firm subject to the Rule that is inconsistent with the information provided by NASD Regulation to the firm that indicated that the firm was not subject to the Rule.

NASD Regulation will compile and maintain several lists that firms will be able to review on a quarterly basis to assist them to determine if they are in compliance with the Rule. The primary list that will be prepared will be a list of firms that meet the definition of Disciplined Firm. Two additional lists will be prepared that should be helpful.

One list will contain an alphabetical listing of all registered persons who had worked for Disciplined Firms within the last three years. Another list will be compiled containing the same list of people grouped according to the firm for which they currently work. In order to alert firms that they are approaching the percentage that would make them subject to the requirements of the Rule, the second list will contain a computation of the percentage of all registered persons at the firm represented by registered persons who had been employed at a Disciplined Firm within the last three years.

The Rule is thus very similar to an NFA interpretation concerning supervision of telemarketing activity.²⁴ NFA member firms subject to the requirements of the interpretation must tape record all sales solicitations. The NFA interpretation applies to firms that meet criteria relating to the percentage of the firm's associated persons who formerly were employed at a firm that was closed down and barred from the industry through enforcement actions for deceptive telemarketing practices.²⁵

These firms are required by the NFA interpretation to tape record sales solicitations. An NFA member subject to these procedures may seek a waiver of the taping requirement upon a satisfactory showing that its current supervisory procedures provide effective supervision over its employees, including enabling the member to identify potential problem areas before customer abuse occurs. The NFA has rarely granted such waivers. In one instance, a waiver was granted to a firm that did not engage in telemarketing and had only institutional customers. In two other instances, partial waivers were granted to firms that hired outside consultants. NFA informed NASD Regulation that they were not satisfied with the work performed by the outside consultants and would not grant such waivers in the future.²⁶ In response to commenter requests, NASD Regulation has included a waiver provision in the proposed Rule, and also has proposed a

¹⁹ See, e.g., letters from AEFA, Duke II, Lawrence, Kamin, Lehman, Morgan Stanley, MSC, Neidiger, Montgomery, SIA, and Smith Barney.

²⁰ See Interpretive Notice to NFA Compliance Rule 2-9, *Supervision of Telemarketing Activity*, §9021 (February 18, 1997).

²¹ 18 U.S.C. §§ 2519 et seq.

²² In one-party statute states, the only issue is whether the registered representative knows of and consents to the tape recording. Since the recording requirement would run to the firm, and the equipment would be the firm's, it might be argued that the firm, and not the representative, is doing the recording. Therefore, it would be necessary for the firm to insure that the representative has notice and consents to the tape recording of his or her telephone conversations. This could be accomplished through a clause in an employment agreement or employee handbook or other written notice to the representative.

²³ In two-party statute states, it would be necessary to insert on the firm's telephone line a recording stating that all telephone conversations are being taped, similar to customer service lines in other industries. Some states require a system of beeps or buzzers that sound throughout the conversation. Another possibility is to insert a clause into the customer agreement notifying customers that their calls will be tape recorded. Some states also have a "business use exception" to the two-party statute consent requirement, but it is worded and applied differently in each state.

²⁴ See Interpretive Notice to NFA Compliance Rule 2-9, *Supervision of Telemarketing Activity*, §9021 (February 18, 1997).

²⁵ In early 1997, 44 firms met the NFA definition of Disciplined Firm. See Interpretive Notice to NFA Compliance Rule 2-9, *Supervision of Telemarketing Activity*, §9021 (February 18, 1997).

²⁶ Telephone conversation between Mary N. Revell, Associate General Counsel, NASD, and Daniel Driscoll, Vice President, Compliance, NFA (February 26, 1997).

conforming change to the Rule 9600 Series.²⁷

III. Discussion

For the reasons discussed below, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and the regulations thereunder applicable to registered securities associations, in particular the requirements of Section 15A(b)(6) of the Act.²⁸ Among other things, Section 15A(b)(6) of the Act requires that the rules of a national securities association be designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and in general, to protect investors and the public interest.

In particular, the Commission believes that the proposed rule change will discourage the revival of disciplined firms that have been barred by the industry or that have had their registrations revoked by the Commission. In essence, firms that decide to hire significant numbers of employees from disciplined firms will be required to ensure a proper supervisory environment that protects investors and prevents fraudulent and manipulative telemarketing acts and practices. The monitoring of registered persons' telephone conversations will help to provide additional supervision of individuals who formerly worked at a disciplined firm where they were inadequately trained and supervised.

In the Notice, the Commission requested comments on all aspects of the proposal, as well as the need to inform investors that their calls are being taped. The Commission received one comment letter concerning the proposal. The SIA expressed general concerns about tape recording conversations as a method of supervision. While the Commission recognizes the limitations of this form of supervision, the Commission believes that if registered persons know their phone calls are being taped then they are more likely to avoid making false or exaggerated representations. In addition, compliance officials will have another tool to monitor persons who worked previously at firms with significant sales practice problems. Moreover, the fact

that tapes of the telephone conversations will be available to persons who have disputes with broker-dealer firms will spur firms with a substantial percentage of representatives from an expelled firm to take extra measures to supervise these persons.

No comments were received concerning the issue of notice to investors that their calls are being taped. NASD Regulation has indicated its belief that the issue of notification is addressed by state privacy laws and that firms will be required to independently determine that state laws are satisfied. The Commission believes that the best practice would be for member firms to notify their registered persons and customers that their telephone calls are being tape recorded.

The Commission expects the NASD to monitor the Rule and assess its effectiveness. For example, the NASD should monitor the number of firms that become subject to the Rule as well as firms that hire representatives from disciplined firms but do not trigger the taping requirement to see if there is a need to adjust the percentages. Also, the NASD should monitor the number of firms exempt from the Rule because they have five or fewer employees to determine if this is an effective exclusion. Furthermore, the NASD should make sure firms comply with state laws on notification.

The Commission finds good cause for approving Amendment No. 2 prior to the thirtieth day after the date of publication of notice thereof in the Federal Register. Amendment No. 2 applies the proposal to member firms with a work force comprised of a specified number of registered persons who were employed by a "disciplined firm" within the last three years instead of two years.²⁹ In the Notice, the Commission requested comment on whether the original two-year time frame was appropriate. Although no comments were received on this issue, NASD Regulation and the Commission believe that a three-year time frame will better capture registered persons who worked at disciplined firms during a period of inadequate training, supervision, and sales practice abuses. Therefore, the Commission believes that granting accelerated approval to Amendment No. 2 is appropriate and consistent with Section 15A of the Act.³⁰

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning Amendment No. 2 to the proposed rule change, 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, N.W., Washington, D.C. 20549. Copies of the submission, all subsequent amendments, all written statements with respect to Amendment No. 2 that are filed with the Commission, and all written communications relating to Amendment No. 2 between the Commission and any persons, 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 will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to File No. SR-NASD-97-69 and should be submitted by May 15, 1998.

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,³¹ that the proposed rule change (SR-NASD-97-69), including Amendment No. 2 thereto, is approved on an accelerated basis.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority,³²

Margaret H. McFarland,
Deputy Secretary.

[FR Doc. 98-10796 Filed 4-22-98; 8:45 am]
BILLING CODE 8010-01-M

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39881; File No. SR-PCX-98-16]

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto by the Pacific Exchange, Inc., Relating to Communication Devices on the Trading Floor

April 16, 1998.

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 March 31, 1998, the Pacific Exchange, Inc. ("PCX"

²⁷ See, e.g., letters from Edwards, Burlington, Cullom, Duke I, Duke II, Duncan-Smith, GKN, Hoak, Morgan Stanley, Baird, and Montgomery.

²⁸ 15 U.S.C. § 78e-3(b)(6).

²⁹ Amendment No. 2 also makes several technical amendments which clarify the application of the previously noticed changes to Rules 3010 and 9610.

³⁰ 15 U.S.C. § 78e-3.

³¹ 15 U.S.C. § 78s(b)(2).

³² 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

24202

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-39883A; File No. SR-NASD-97-69]

Self-Regulatory Organizations; Order Granting Approval of Proposed Rule Change, as Amended, and Notice of Filing and Order Granting Accelerated Approval of Amendment No. 2 to the Proposed Rule Change by the National Association of Securities Dealers, Inc., Relating to the Tape Recording of Conversations

April 23, 1998.

Correction

In FR Document No. 98-10796, beginning on page 20232 for Tuesday, April 23, 1998, make the following correction. On page 20235, second column, the first full paragraph, revise the second sentence to read:

"The procedures would require, at a minimum, that the member tape record all telephone conversations between all of its registered persons and both existing and potential customers for a period of two years, and maintain these supervisory procedures for two years."

Jonathan G. Katz,

Secretary.

[FR Doc. 98-11567 Filed 4-30-98; 8:45 am]

BILLING CODE 8010-01-M

SMALL BUSINESS ADMINISTRATION

Data Collection Available for Public Comments and Recommendations

ACTION: Notice and request for comments.

SUMMARY: In accordance with the Paperwork Reduction Act of 1995, this notice announces the Small Business Administration's intentions to request approval on a new, and/or currently approved information collection.

DATES: Comments should be submitted on or before June 30, 1998.

FOR FURTHER INFORMATION CONTACT: Curtis B. Rich, Management Analyst, Small Business Administration, 409 3rd Street, S. W., Suite 5000, Washington, D. C. 20416. Phone Number: 202-205-6629.

SUPPLEMENTARY INFORMATION:

Title: "8 (a) Export Survey Initiative".
Type of Request: New Request.
Form No: N/A.

Description of Respondents: 8 (a) Firms who are located in the top ten exporting states and have more than one

of the SIC Codes listed as the top ten for exporting.

Annual Responses: 200.

Annual Burden: 50.

Comments: Send all comments regarding this information collection to William A. Fisher, Acting Associate Administrator, Office of Minority Enterprise Development, Small Business Administration, 409 3rd Street, S.W., Suite 8000, Washington, D.C. 20416. Phone No: 202-205-6412.

Send comments regarding whether this information collection is necessary for the proper performance of the function of the agency, accuracy of burden estimate, in addition to ways to minimize this estimate, and ways to enhance the quality.

Dated: April 27, 1998.

Jacqueline White,

Chief, Administrative Information Branch.

[FR Doc. 98-11540 Filed 4-30-98; 8:45 am]

BILLING CODE 8025-01-P

SMALL BUSINESS ADMINISTRATION

[Declaration of Economic Injury Disaster #9841]

Commonwealth of Pennsylvania and Contiguous Counties in Ohio

Mercer County and the contiguous Counties of Butler, Crawford, Lawrence, and Venango in Pennsylvania and Mahoning and Trumbull Counties in Ohio constitute an economic injury disaster loan area as a result of a fire that occurred on April 6, 1998 in the Hermitage Square Plaza in the City of Hermitage, Pennsylvania. Eligible small businesses and small agricultural cooperatives without credit available elsewhere may file applications for economic injury assistance as a result of this disaster until the close of business on January 25, 1999 at the address listed below or other locally announced locations: Small Business Administration, Disaster Area 1 Office, 360 Rainbow Blvd. South, 3rd Fl., Niagara Falls, NY 14303.

The interest rate for eligible small businesses and small agricultural cooperatives is 4 percent.

The economic injury number for Ohio is 9842002.

(Catalog of Federal Domestic Assistance Program No. 59002)

Dated: April 23, 1998.

Aida Alvarez,

Administrator.

[FR Doc. 98-11539 Filed 4-30-98; 8:45 am]

BILLING CODE 8025-01-P

SMALL BUSINESS ADMINISTRATION

[Declaration of Disaster #3079]

Arkansas; (and Contiguous Counties in Missouri and Tennessee)

Mississippi County and the contiguous Counties of Craighead, Crittenden, and Poinsett in the State of Arkansas; Dunklin and Pemiscot Counties in the State of Missouri; and Dyer, Lauderdale, and Tipton Counties in the State of Tennessee constitute a disaster area as a result of damages caused by severe storms and tornadoes that occurred on April 16, 1998. Applications for loans for physical damages as a result of this disaster may be filed until the close of business on June 22, 1998 and for economic injury until the close of business on January 25, 1999 at the address listed below or other locally announced locations: Small Business Administration, Disaster Area 3 Office, 400 Amon Carter Blvd., Suite 102, Ft. Worth, TX 76155.

The interest rates are:

	Percent
For Physical Damage:	
Homeowners With Credit Available Elsewhere	7.000
Homeowners Without Credit Available Elsewhere	3.500
Businesses With Credit Available Elsewhere	8.000
Businesses and Non-Profit Organizations Without Credit Available Elsewhere	4.000
Others (Including Non-Profit Organizations) With Credit Available Elsewhere	7.125
For Economic Injury:	
Businesses and Small Agricultural Cooperatives Without Credit Available Elsewhere	4.000

The numbers assigned to this disaster for physical damages are 307912 for Arkansas; 308012 for Missouri; and 308112 for Tennessee. For economic injury the numbers are 984300 for Arkansas; 984400 for Missouri; and 984500 for Tennessee.

(Catalog of Federal Domestic Assistance Program Nos. 59002 and 59008)

Dated: April 23, 1998.

Aida Alvarez,

Administrator.

[FR Doc. 98-11538 Filed 4-30-98; 8:45 am]

BILLING CODE 8025-01-P

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS, EASTERN DIVISION

NEIL J. ASLIN, individually and on behalf of all others similarly situated,)	
)	
Plaintiff,)	
)	Case No.
v.)	
)	
Financial Industry Regulatory Authority, Inc., a Delaware not-for-profit corporation,)	
)	
Defendant.)	

AFFIDAVIT OF JENNIFER M. MUCHONEY

NOW COMES JENNIFER M. MUCHONEY, the Affiant herein, who first being duly sworn, states that she is an adult under no disability who is willing and able to testify in this Court to the facts stated herein, which are offered of her own personal knowledge and recall as follows:

1. I have been a practicing attorney in the State of Illinois for over eight years, and I have personal knowledge of the matters stated herein.
2. On June 13, 2011, I spoke with Ms. Patricia Albrecht in the Financial Industry Regulatory Authority, Inc. (“FINRA”) Office of General Counsel, and inquired as to whether there was any mechanism at FINRA by which individual brokers might remove themselves from inclusion as a “tainted” registrant on a FINRA notice to a member firm requiring said firm to either conform to the numerical limitations of FINRA Rule 3010(b)(2)(H) or to reduce its staffing level.
3. Ms. Albrecht informed me that there was no such mechanism at FINRA for individual persons.

4. FURTHER AFFIANT SAYETH NOT.


Jennifer M. Muchoney

Subscribed and sworn to before me
this 15th day of June, 2011.


Notary Public

