

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-52165; File No. SR-PCX-2005-80]

### Self-Regulatory Organizations; Pacific Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change and Amendment Nos. 1 and 2 Thereto Relating to the Continuing Education Regulatory Element Requirement

July 29, 2005.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 8, 2005, the Pacific Exchange, Inc. ("PCX" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in items I, II and III below, which Items have been prepared by the Exchange. On July 13, 2005, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>3</sup> On July 21, 2005, the Exchange filed Amendment No. 2 to the proposed rule change.<sup>4</sup> The PCX has filed the proposal as a "non-controversial" rule change pursuant to section 19(b)(3)(A) of the Act<sup>5</sup> and Rule 19b-4(f)(6) thereunder,<sup>6</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change, as amended, from interested persons.

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

The PCX proposes to amend PCX Rule 9.27 to eliminate the "Grandfather" exemption to the regulatory element of the Continuing Education ("CE") Program. Below is the text of the proposed rule change. Proposed new

language is in *italics*. Deletions are in [brackets].

#### Rules of the Pacific Exchange, Inc.

##### Rule 9

Rule 9.27(a)-(b)—No Change.

Rule 9.27(c)—No OTP Firm or OTP Holder shall permit any registered person to continue to, and no registered person shall continue to, perform duties as a registered person, unless such person has complied with the continuing education requirements of this Rule 9.27(c).

Each registered person shall complete the Regulatory Element of the continuing education program beginning with the occurrence of their second registration anniversary date, and every three years thereafter, or as otherwise prescribed by the Exchange. On each occasion, the Regulatory Element must be completed within one hundred twenty days after the person's registration anniversary date. A person's initial registration date, *also known as the "base date"*, shall establish the cycle anniversary dates for purposes of this Rule. The content of the Regulatory Element of the program shall be determined by the Exchange for each registration category of persons subject to the Rule.

(1) *Reserved*. [Persons who have been continuously registered for more than ten years as of the effective date of this Rule are exempt from the requirements of this rule relative to participation in the Regulatory Element of the continuing education program, provided such persons have not been subject to any disciplinary action within the last ten years as enumerated in subsection (c)(3)(i)-(ii) of this Rule. However, persons delegated supervisory responsibility or authority pursuant to Rule 9.8 and registered in such supervisory capacity are exempt from participation in the Regulatory Element under this provision only if they have been continuously registered in a supervisory capacity for more than 10 years as of the effective date of this Rule and provided that such supervisory person has not been subject to any disciplinary action under subsection (c)(3)(i)-(ii) of this Rule.]

In the Event that a registered person who is exempt from participation in the Regulatory Element subsequently becomes the subject of a disciplinary action as enumerated in subsection (c)(3)(i)-(ii), such person shall be required to satisfy the requirements of the Regulatory Element as if the date the disciplinary action becomes final is the person's initial registration anniversary date.]

(2) Failure to Complete—Unless otherwise determined by the Exchange, any registered persons who have not completed the Regulatory Element of the program within the prescribed time frames will have their registration deemed inactive until such time as the requirements of the program have been satisfied. Any person whose registration has been deemed inactive under this Rule shall cease all activities as a registered person and shall be prohibited from performing any duties and functioning in any capacity requiring registration.

The Exchange may, upon application and a showing of good cause, allow for additional time for a registered person to satisfy the program requirements.

(3) *Disciplinary Actions* [Re-entry into Program]—Unless otherwise determined by the SRO, a registered person will be required to [re-enter] *re-take* the Regulatory Element and satisfy all of its requirements in the event such person:

(A) becomes subject to any statutory disqualification as defined in Section (3)(a)(39) of the Securities Exchange Act of 1934;

(B) becomes subject to suspension or to the imposition of a fine of \$5,000 or more for violation of any provision of any securities law or regulation, or any agreement with or rule of standard of conduct of any securities governmental agency, securities self-regulatory organization, or as imposed by any such regulatory or self-regulatory organization in connection with a disciplinary proceeding; or

(C) is ordered as a sanction in a disciplinary action to [re-enter] *re-take* the [continuing education program] *Regulatory Element* by any securities governmental agency or securities self-regulatory organization.

[Re-entry into the program] *A re-taking of the Regulatory Element* shall commence with [the initial] participation within 120 days of the registered person becoming subject to the statutory disqualification, in the case of ([i]A) above, or the disciplinary action becoming final, in the case of ([ii]B) or ([iii]C) above. *The date that the disciplinary action becomes final will be deemed the person's new base date for purposes of this Rule.*

Rule 9.27(d)—Commentary .02—No Change.

Commentary .03—Any registered person who has terminated association with a registered broker or dealer and who has, within two years of the date of termination, become reassociated in a registered capacity with a registered broker or dealer shall participate in the Regulatory Element of the continuing education program at such intervals that

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

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

<sup>3</sup> In Amendment No. 1, the Exchange added language to its rule text to make PCX rules consistent with the rules of the other self-regulatory organizations ("SROs") and added clarifying language to the purpose section.

<sup>4</sup> In Amendment No. 2, the Exchange made minor edits to the rule text and withdrew its request to have the Commission waive the 30 day operative period. The effective date of the original proposed rule change is July 8, 2005, the effective date of Amendment No. 1 is July 13, 2005 and the effective date of Amendment No. 2 is July 21, 2005. For purposes of calculating the 60-day period within which the Commission may summarily abrogate the proposed rule change, as amended, under Section 19(b)(3)(C) of the Act, the Commission considers such period to commence on July 21, 2005, the date on which the Exchange filed Amendment No. 2. See 15 U.S.C. 78s(b)(3)(C).

<sup>5</sup> 15 U.S.C. 78s(b)(3)(A).

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

apply (second registration anniversary and every three years thereafter) based on the [initial registration anniversary] *new base date*, rather than based on the date of reassociation in a registered capacity. Any former registered person who becomes reassociated in a registered capacity with a registered broker or dealer more than two years after termination as such will be required to satisfy the program's requirements in their entirety based on the most recent registration date.

\* \* \* \* \*

Commentary .05—*Reserved*. [The effective date of this Rule, for the purposes of determining whether a registered person is exempt from participation in the Regulatory Element is September 14, 2000.]

Commentary .06—*Any registered member who is an OTP Holder who is also a member of another self-regulatory organization ("SRO") shall be subject to the other SRO's implementation date for the elimination of the exceptions to the Regulatory Element section of the continuing education program, if that date is earlier than September 30, 2005.*

## II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change, as amended, and discussed any comments it received on the proposed rule change, as amended. The text of these statements may be examined at the places specified in item IV below. The PCX has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

#### 1. Purpose

The Exchange proposes to amend PCX Rule 9.27 to eliminate all exemptions from the Exchange Continuing Education Regulatory Element Program for registered representatives to conform its PCX Rule 9.27 with applicable rules of other SROs. Currently PCX Rule 9.27 sets forth the rules governing the requirements for registered representatives to participate in the Continuing Education Regulatory Element Program (the "Regulatory Element").<sup>7</sup> The Regulatory Element is a

computer-based education program administered by the National Association of Securities Dealers ("NASD") to help ensure that registered persons are kept up-to-date on regulatory, compliance and sales practices in the industry. PCX Rule 9.27 specifies the Continuing Education ("CE") requirements for registered persons subsequent to their initial qualification and registration with the PCX. Unless exempt, each registered person is required to complete the Regulatory Element within 120 days after the person's second anniversary date and, thereafter within 120 days after every third registration anniversary date. There are three Regulatory Element programs: the S201 Supervisor Program for registered principals and supervisors, the S106 Series 6 Program for Series 6 representatives, and the S101 General Program for Series 7 and all other registrations.

According to the NASD, approximately 135,000 registered persons are exempt from the Regulatory Element. These include registered persons who, when the Continuing Education Program was adopted in 1995, had been registered for at least ten years and who did not have a significant disciplinary action<sup>8</sup> in the CRD record for the previous ten years (so-called "grandfathered" persons). These also include those persons who had "graduated" from the Regulatory Element by satisfying their tenth anniversary requirement before July 1998, when PCX Rule 9.27 was amended and the graduation provision eliminated, and who did not have a significant disciplinary action in their CRD record for the previous ten years.<sup>9</sup>

Exchange Firm Element of the Continuing Education Program applies to any person registered with an NASD member firm who has direct contact with customers in the conduct of the member's securities sales, trading and investment banking activities, any person registered as a research analyst pursuant to NASD Rule 1050, and to the immediate supervisors of such persons (collectively called "covered registered persons"). The requirement stipulates that each member firm must maintain a continuing and current education program for its covered registered persons to enhance their securities knowledge, skill and professionalism. Each firm has the requirement to annually conduct a training needs analysis, develop a written training plan, and implement the plan.

<sup>8</sup> For purposes of PCX Rule 9.27(c), a significant disciplinary action generally means a statutory disqualification, a suspension or imposition of a fine of \$5,000 or more, or being subject to an order from a securities regulator to re-take the Regulatory Element. See PCX Rule 9.27(c)(3).

<sup>9</sup> When PCX Rule 9.27 was first adopted in 1995, the Regulatory Element required registered persons to satisfy the Regulatory Element on the second, fifth, and tenth anniversary of their initial securities registration. After satisfying the tenth anniversary requirement, a person was "graduated" from the Regulatory Element. A graduated person who was

At its December 2003 meeting, the Securities Industry/Regulatory Council on Continuing Education ("Council") discussed the current exemptions from the Regulatory Element and agreed unanimously to recommend that the SROs repeal the exemptions and require all registered persons to participate in the Regulatory Element. In reaching this conclusion, the Council was of the view that there is great value in exposing all industry participants to the benefits of the Regulatory Element, in part because of the significant regulatory issues that have emerged over the past few years. The Regulatory Element programs include teaching and training content that is continuously updated to address current regulatory concerns as well as new products and trading strategies. Exempt persons presently do not have the benefit of this material.

In addition, the Council will introduce a new content module to the Regulatory Element programs that will specifically address ethics and will require participants to recognize ethical issues in given situations. Participants will be required to make decisions in the context of, for example, peer pressure, the temptation to rationalize, or a lack of clear-cut guidelines from existing rules or regulations. The Council strongly believes that all registered persons, regardless of their years of experience in the industry, should have the benefit of this training.

Consistent with the Council's recommendation, the proposed rule change, as amended, would eliminate the current Regulatory Element exemptions. The other SRO members of the Council also support eliminating the exemptions and either have already or are pursuing amendments to their respective rules.

The effective date of the proposed rule change, as amended, will be September 30, 2005.<sup>10</sup> PCX will announce the effective date of the proposed rule change in the PCX Weekly Bulletin following the effective date of the proposed rule, as amended.

Moreover, following the effective date of the proposed rule change, as

not a principal re-entered if he or she acquired a principal registration or incurred a significant disciplinary action.

<sup>10</sup> To eliminate any confusion, the Exchange has confirmed in the proposed rule change that an Exchange participant who is also a member of another SRO must comply with the rules of the other SRO which eliminated these exceptions as of an earlier date. See Securities Exchange Act Release Nos. 50404 (September 16, 2004), 69 FR 57126 (September 23, 2004); 50456 (September 27, 2004), 69 FR 59285 (October 4, 2004); 50630 (November 3, 2004), 69 FR 65232 (November 10, 2004); and 50651 (November 10, 2004) 69 FR 67374 (November 17, 2004).

<sup>7</sup> The Continuing Education Program also has a "Firm Element." See PCX Rule 9.27(d). The

amended, implementation will be based on the application of the existing requirements of the Regulatory Element to all registered persons. The way in which the Web Central Registration Depository ("Web CRD"), which is administered by the NASD, applies these requirements is as follows. Web CRD establishes a "base date" for each registered person and calculates anniversaries from that date. Usually, the base date is the person's initial securities registration. However, the base date may be revised to be the effective date of a significant disciplinary action in accordance with PCX Rule 9.27 or the date on which a formerly registered person re-qualifies for association with a PCX OTP Holder or OTP Firm by qualification exam. Using the base date, Web CRD creates a Regulatory Element requirement on the second anniversary of the base date and then every three years thereafter. Registered persons formerly exempt from the Regulatory Element requirement must satisfy this requirement that occurs on an anniversary on or after the effective date of the proposed rule change, as amended.

It is noted that a person's base date may be revised to be the effective date of a significant disciplinary action in accordance with PCX Rule 9.27. The Exchange proposes to amend PCX Rule 9.27 to clarify that a person subject to a significant disciplinary action would be required to "re-take" rather than "re-enter" the Regulatory Element.<sup>11</sup> A person's base date may also be revised to be the date on which a formerly registered person re-qualifies for association with an OTP Holder or OTP Firm.

## 2. Statutory Basis

The Exchange believes that the proposed rule change, as amended, is consistent with section 6(b)<sup>12</sup> of the Act, in general, and furthers the objectives of section 6(b)(5),<sup>13</sup> in particular, in that it is designed to facilitate transactions in securities, to promote just and equitable principles of trade, to foster competition, and to protect investors and the public interest. The Exchange believes that the proposed rule change is designed to accomplish these ends by ensuring that all registered persons are kept up-to-date on industry rules, regulations, and practices.

<sup>11</sup> This requirement would apply to all registered persons that are subject of a significant disciplinary action, and not only to currently exempt persons.

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

<sup>13</sup> 15 U.S.C. 78f(b)(5).

Additionally, under section 6(c)(3)(B) of the Act,<sup>14</sup> the Exchange may bar a natural person from becoming a member or person associated with a member, if such natural person does not meet such standards of training, experience, and competence as prescribed by the rules of the Exchange. Pursuant to this statutory obligation, the Exchange is rescinding all exemptions from the requirement to complete the Regulatory Element of the Continuing Education Program as prescribed by Exchange Rule 9.27.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

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

Written comments on the proposed rule change were neither solicited nor received.

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

Because the foregoing proposed rule change, as amended: (1) Does not significantly affect the protection of investors or the public interest; (2) does not impose any significant burden on competition; and (3) does not become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to section 19(b)(3)(A) of the Act<sup>15</sup> and Rule 19b-4(f)(6) thereunder.<sup>16</sup>

At any time within 60 days of the filing of such proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and

<sup>14</sup> 15 U.S.C. 78f(c)(3)(B).

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

<sup>16</sup> 17 CFR 240.19b-4(f)(6). Rule 19b-4(f)(6) also requires that the exchange give the Commission written notice of its intent to file the proposed rule change along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing the proposed rule change. The Exchange satisfied this requirement.

arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

### Electronic Comments

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-PCX-2005-80 on the subject line.

### Paper Comments

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE., Washington, DC 20549-9303.

All submissions should refer to File Number SR-PCX-2005-80. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of the filing also will be available for inspection and copying at the principal offices of the PCX. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-PCX-2005-80 and should be submitted on or before August 26, 2005.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>17</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

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**BILLING CODE 8010-01-P**

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