

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49119; File Nos. SR-NASD-2004-03; SR-NASD-2004-10; SR-NYSE-2004-01]

### Self-Regulatory Organizations; Notice of Filing and Immediate Effectiveness of Proposed Rule Changes by the National Association of Securities Dealers, Inc. and the New York Stock Exchange, Inc. Relating To Establishing Effective Dates for Certain Provisions of NASD Rule 2711 and NASD Rule 1050 and Certain Provisions of NYSE Rule 472 and NYSE Rule 344

January 23, 2004.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Exchange Act" or "Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on January 9, 2004 and on January 16, 2004, the National Association of Securities Dealers, Inc. ("NASD"), and on January 16, 2004, the New York Stock Exchange, Inc. ("NYSE" or "Exchange"), filed with the Securities and Exchange Commission ("SEC" or "Commission") proposed rule changes as described in Items I, II, and III below, which Items have been prepared by the respective self-regulatory organizations ("SROs").

The SROs have designated the proposed rule changes as constituting a stated policy, practice, or interpretation with respect to the meaning, administration, or enforcement of an existing rule series under paragraph (f)(1) of Rule 19b-4 under the Act,<sup>3</sup> which renders the proposals effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule changes from interested persons.

#### I. Self-Regulatory Organizations' Statements of the Terms of Substance of the Proposed Rule Changes

NASD is filing with the SEC a proposed rule change to establish April 26, 2004 as the effective date for the recently amended provisions of NASD Rule 2711(h)(2) that require certain disclosures by members and research analysts of compensation received by the member or its affiliates from the subject company of a research report or public appearance.

NASD is also filing with the SEC a proposed rule change to establish "not later than March 30, 2004" as the effective date for Rule 1050, which

requires persons associated with a member who function as research analysts to be registered as such and to pass a qualification examination. The proposal also would ensure that the effective date for Rule 1050 would occur no sooner than 30 days after a study outline for the Research Analyst Qualification Examination is filed by NASD with the Commission and becomes effective.

The NYSE is filing with the SEC a proposed rule change that would change the effective date for certain provisions of Rule 472 ("Communications with the Public") and Rule 344 ("Research Analysts and Supervisory Analysts").

#### II. Self-Regulatory Organizations' Statements of the Purpose of, and Statutory Basis for, the Proposed Rule Changes

In their filings with the Commission, NASD and the NYSE included statements concerning the purpose of and basis for the proposed rule changes. The text of these statements may be examined at the places specified in Item IV below. NASD and the NYSE have prepared summaries, set forth in Sections A, B, and C below.

##### A. Self-Regulatory Organizations' Statements of the Purpose of, and Statutory Basis for, the Proposed Rule Changes

###### 1. NASD's Purpose

NASD is filing the proposed rule change to establish April 26, 2004 as the effective date for the recently amended provisions of NASD Rule 2711(h)(2) that require disclosure of compensation received by the member and its affiliates from the subject company of a research report or public appearance. The SEC approved these amendments to Rule 2711 on July 29, 2003 as part of a proposal that augmented research analyst conflicts of interest rules generally and imposed registration and continuing education requirements on research analysts.<sup>4</sup>

Generally, the amendments to Rule 2711(h)(2) require a member to disclose in a research report (1) non-investment banking compensation received by it or its affiliates from a subject company in the past 12 months and (2) if a subject company is, or during the past 12-month period, was a client of the member and types of client services provided to the subject company. The amendments further require a research analyst to disclose in a public appearance (1) if, to the extent the

analyst knows or has reason to know, the member or an affiliate received any compensation in the past 12 months, (2) if the research analyst received any compensation from the subject company in the past 12 months, and (3) if, to the extent the analyst knows or has reason to know, a subject company is, or during the past 12-months period was, a client of the member and types of client services provided to the subject company. These provisions supplement requirements in Rule 2711(h)(2) that require disclosure of investment banking compensation received or sought by a member from a subject company and any compensation received by a research analyst that is based upon a member's investment banking services revenues.

The July Approval Order established a January 26, 2004 as the effective date for the new compensation disclosure provisions, but also provided that NASD may grant an additional 90 days to comply as it deems necessary on a case-by-case basis.<sup>5</sup> Thus, NASD believes that the approval order recognized that additional time might be necessary for some or all members to put systems in place to track various types of compensation and client relationships required to be disclosed under the new provisions.

According to NASD, it has received several requests from members to extend the implementation date of these provisions due to the scope and difficulty required to implement the technology, systems and other changes needed to achieve compliance with the non-investment banking compensation and client disclosure provisions. According to NASD, its members noted the rule requirements necessitate that they build and test new systems and technology feeds to aggregate data across a wide range of business lines within the members. Moreover, in many instances, members must extend that technological infrastructure to global affiliates. According to NASD, members also noted that the timing of the implementation date overlaps with year-end technology "freezes" that many firms impose to ensure that systems changes do not impact the accuracy of year-end information gathering related to financial reporting and taxes.

NASD believes these members have demonstrated good cause for an extension of the effective date for the applicable provisions. Moreover, NASD believes the problems cited by the

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

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

<sup>3</sup> 17 CFR 240.19b-4(f)(1).

<sup>4</sup> See Securities Exchange Act Release No. 48252 (July 29, 2003), 68 FR 45875 (August 4, 2003) ("July Approval Order").

<sup>5</sup> Since the 90th day after the current effective date is a Sunday (April 25, 2004), the proposed rule change would establish the compliance date as the following Monday, April 26, 2004.

requesting members are common within the industry and that there should be a uniform effective date for all members. Therefore, NASD is establishing April 26, 2004 as the effective date for the new provisions of Rule 2711(h)(2) for all members. NASD notes that all existing provisions under Rule 2711(h)(2) remain in effect and are not subject to the new effective date.

NASD is also filing the proposed rule change to establish "not later than March 30, 2004" as the effective date for Rule 1050, which requires that any person associated with a member who functions as a "research analyst" be registered as such and pass a qualification examination. For the purposes of Rule 1050, "research analyst" means an associated person who is primarily responsible for the preparation of the substance of a research report or whose name appears on a research report.

In the July Approval Order, the SEC approved NASD Rule 1050 on July 29, 2003, together with amendments to NASD Rules 2711 and 1120 that augmented research analyst conflicts of interest rules generally and imposed registration and continuing education requirements on research analysts. The July Approval Order established January 26, 2004, or "such later date as determined by NASD" as the effective date for the Rule 1050 registration provision. Thus, NASD believes that the approval order recognized that additional time might be necessary to fully develop the examination and complete the attendant administrative requirements necessary to begin registration and testing.

According to NASD, it has been working diligently with NYSE to develop and implement the qualification examination required by Rule 1050 and NYSE's corresponding Rule 344. As a result, NASD believes that it will shortly file with the Commission the study outline and specifications of the examination. According to NASD, NASD intends to submit to the Commission shortly a proposed rule change that would set forth certain prerequisites and exemptions to the registration and qualification requirements. According to NASD, a fee filing also will follow separately. Therefore, NASD is proposing to establish an effective date of "not later than March 30, 2004" for Rule 1050 to allow sufficient time for (1) consideration of, and action on, the aforementioned proposed rule changes by the Commission and (2) members to prepare their research analysts to take the examination after a study outline is filed with the Commission and made

effective. In furtherance of the latter, NASD also is proposing that the effective date be set no sooner than 30 days after the Commission acts on a study outline for the Research Analyst Qualification Examination.

## 2. NASD's Statutory Basis

NASD believes that the proposed rule changes are consistent with the provisions of section 15A(b)(6) of the Act,<sup>6</sup> which requires, among other things, that NASD rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that the proposed rule change (SR-NASD-2004-03) will further investor protection by giving members adequate time to establish systems that can effectively track information that will reduce or expose conflicts of interest and thereby significantly curtail the potential for fraudulent and manipulative acts.

NASD also believes that this proposed rule change (SR-NASD-2004-10) will foster greater investor protection by providing adequate time for the development of a comprehensive research analyst competency examination and for members to prepare their research analysts for such examination.

## 3. NYSE's Purpose

The NYSE is filing the proposed rule change to extend by 90 calendar days the effective date for the recently amended provisions of NYSE Rule 472(k)(1), (2) and (3) ("Disclosure Provisions") that relate to compensation received by a member and its affiliates from the subject company of a research report or public appearance.<sup>7</sup> In addition, the Exchange is also proposing to establish "not later than March 30, 2004," as the effective date for the recently amended provision of NYSE Rule 344, which requires research analysts to be registered with and qualified by the Exchange.

## Background

In the July Approval Order, the Commission approved amendments to Exchange Rule 472 ("Communications with the Public"), Rule 351 ("Reporting Requirements"), Rule 344 ("Supervisory Analysts"), and Rule 345A ("Continuing Education for Registered Persons").

The Exchange proposed these additional amendments: (1) To enhance the SRO Rules approved in May 2002<sup>8</sup> and (2) to comply with the mandate of the Sarbanes-Oxley Act of 2002 ("SOA").<sup>9</sup>

## Disclosure Provisions

The amendments require a member or member organization to disclose in a research report (1) non-investment banking compensation received by it or its affiliates from the subject company in the past 12 months, and (2) if a subject company is, or during the past 12-month period was, a client of the member or member organization and the types of client services provided to the subject company.

The amendments further require a research analyst to disclose in a public appearance (1) if, to the extent the analyst knows or has reason to know, the member or member organization or its affiliate received any compensation from the subject in the past 12 months, (2) if the research analyst received any compensation from the subject company in the past 12 months, and (3) if, to the extent the analyst knows or has reason to know, if the subject company is, or during the past 12-month period, was a client of the member and the types of client services provided to the subject company. These provisions supplement requirements in Rule 472(k)(1) that require disclosure of investment banking compensation received, sought or expected to be received by a member or member organization or its affiliate from a subject company and any compensation received by a research analyst that is based upon a member's or member organization's investment banking services revenues.

The July Approval Order established a January 26, 2004 implementation date for the Disclosure Provisions, but also provided the Exchange with the discretion to grant, upon written request, an additional 90 days to members and member organizations to comply as it deems necessary on a case-by-case basis. NYSE believes that implicit in the Commission's approval order was the recognition that additional time might be necessary for some or all members to implement systems to track various types of compensation and client relationships required to be disclosed under the new Disclosure Provisions required by the SOA.

<sup>8</sup> See Securities Exchange Act Release No. 45908 (May 10, 2002); 67 FR 34969 (May 16, 2002).

<sup>9</sup> See Pub. L. 107-204, 116 Stat. 745 (2002). The SOA amends the Exchange Act by adding new section 15D. See 15 U.S.C. 78a *et seq.*; 15 U.S.C. 78o-6.

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

<sup>7</sup> NYSE Rule 472(k)(1)(i)d., (k)(1)(ii)a.1. and b., (k)(1)(iii)a., 472(k)(2)(i)c., (k)(2)(i)f. and the exceptions to these disclosure provisions pursuant to Rule 472(k)(3)(i).

According to NYSE, the Exchange received numerous requests from members and member organizations to extend the implementation date of these provisions due to the scope and difficulty required to implement the technology, systems and other changes needed to achieve compliance with the non-investment banking compensation and client disclosure provisions. Members and member organizations noted that the rule requirements necessitate that they build and test new systems and technology feeds to aggregate data across a wide range of business lines within the members. Moreover, in many instances, members and member organizations must extend that technological infrastructure to global affiliates. In addition, members and member organizations noted that the timing of the implementation date overlaps with year-end technology "freezes" that many firms impose to ensure that systems changes do not impact the accuracy of year-end information gathering related to financial reporting and taxes.

The Exchange believes that these members and member organizations have provided sufficient justification for an across-the-board extension of the effective date for the applicable provisions. Moreover, the NYSE believes the problems cited by the requesting members and member organizations are endemic to the industry and that there should be a uniform effective date for all members. Therefore, the Exchange is establishing April 26, 2004<sup>10</sup> as the effective date for the new Disclosure Provisions. Existing provisions under Rule 472(k)(1), (2) and (3) remain in effect and are not subject to the new effective date.

#### Research Analyst Qualification Examination

As noted above, in the July Approval Order, the SEC approved a new Research Analyst Qualification Examination requirement for Research Analysts primarily responsible for the preparation of the substance of research reports and/or whose names appear on such reports (Rule 344.10). Accordingly, such analysts must pass a qualification examination that was scheduled for implementation on January 26, 2004.

The Exchange is establishing "not later than March 30, 2004" as the effective date for the examination. The effective date for the new Research Analyst Qualification examination pursuant to Rule 344 would also not

occur sooner than 30 days after the study outline, which NYSE believes it will file with the Commission, becomes effective. The NYSE believes that the extension is necessary to permit the Exchange to make the requisite filings regarding the study outline for the examination, certain pre-requisites to and exemptions from the examination, and fees associated with its administration.

#### 4. NYSE's Statutory Basis

The statutory basis for the proposed rule change is section 6(b)(5) of the Exchange Act<sup>11</sup> which requires, among other things, that the rules of the Exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade and in general to protect investors and the public interests.

#### *B. Self-Regulatory Organizations' Statements on Burden on Competition*

NASD and NYSE do not believe that the proposed rule changes will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Exchange Act, as amended.

#### *C. Self-Regulatory Organizations' Statements on Comments on the Proposed Rule Changes Received From Members, Participants or Others*

The NASD and NYSE have neither solicited nor received written comments on the proposed rule changes.

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

The proposed rule changes have been filed by NASD and NYSE as stated policies, practices, or interpretations with respect to the meaning, administration, or enforcement of an existing rule series under Rule 19b-4(f)(1) under the Act.<sup>12</sup> Consequently, they have become effective pursuant to section 19(b)(3)(A)<sup>13</sup> of the Act and Rule 19b-4(f)(1) thereunder.<sup>14</sup>

At any time within 60 days of this filing, the Commission may summarily abrogate these proposals 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 Exchange Act.

#### **IV. Solicitation of Comments**

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule changes are consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549-0609. Comments may also be submitted electronically at the following e-mail address: [rule-comments@sec.gov](mailto:rule-comments@sec.gov). All comment letters should refer to File Nos. SR-NASD-2004-03, SR-NASD-2004-10, and SR-NYSE-2004-01. These file numbers should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, comments should be sent in hard copy or by e-mail but not by both methods.

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule changes that are filed with the Commission, and all written communications relating to the proposed rule changes 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 such filings will also be available for inspection and copying at the principal offices of the NASD and NYSE. All submissions should refer to the file numbers SR-NASD-2004-03, SR-NASD-2004-10, and SR-NYSE-2004-01 and should be submitted by February 19, 2004.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>15</sup>

**Margaret H. McFarland,**

*Deputy Secretary.*

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#### **SOCIAL SECURITY ADMINISTRATION**

##### **Agency Information Collection Activities: Proposed Request and Comment Request**

The Social Security Administration (SSA) publishes a list of information collection packages that will require clearance by the Office of Management and Budget (OMB) in compliance with Pub. L. 104-13, the Paperwork Reduction Act of 1995, effective October

<sup>10</sup> Since 90 days would provide for effectiveness on April 25, 2004 (a Sunday), the actual effective date would be Monday, April 26.

<sup>11</sup> 15 U.S.C. 78f(b)(5).

<sup>12</sup> 17 CFR 240.19b-4(f)(1).

<sup>13</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>14</sup> 17 CFR 240.19b-4(f)(1).

<sup>15</sup> 17 CFR 200.30-3(a)(12).