

NASD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

March 12, 1975

TO: All NASD Member Firms

ATTENTION: Training Personnel and Registration Departments

Effective immediately for the Series #7 Qualification Examination for General Securities Registered Representatives and beginning on May 1, 1975, for all other examinations administered by the NASD, the Association will no longer utilize the facilities of United States embassies and consulates to conduct its foreign qualification examination program.

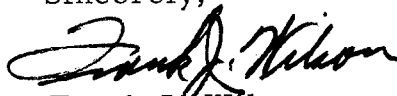
Instead, the Association will conduct regularly scheduled examination sessions on the third Saturday of alternate months at two locations in Europe-- Paris, France and Frankfurt, Germany--and at one location in the Far East-- Tokyo, Japan. All examinations administered at these centers will be on an appointment basis only, will require the submission of a special Foreign Examination Request Form to the NASD for each candidate at least four weeks in advance of a scheduled session and the pre-payment of a \$15.00 per session per candidate foreign administrative fee before the required appointment will be made.

Upon request the Association will attempt to arrange special examination sessions in other areas of the world such as South America, the Middle East, and Australia, but cannot guarantee that suitable arrangements can be made. Requests for appointment sessions in these locations should be submitted at least eight weeks in advance of the desired date. Additional costs incurred by the Association in making such arrangements will be billed to the candidate's sponsoring firm.

Test centers which the Association has maintained in Canada will continue to be part of the Association's examination program and will be administered in the same manner as test centers in the United States. Candidates who intend to sit for examinations in Canada need not submit Foreign Examination Request Forms to the NASD.

For complete details on the procedures to be followed when requesting foreign examination appointments and in order to obtain a supply of Foreign Examination Request Forms, contact Ms. Janet G. Hale, Assistant Director, Examinations at (202) 833-7174.

Sincerely,



Frank J. Wilson  
Senior Vice President  
Regulation

**NASD**

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.  
 1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

March 13, 1975

TO: All NASD Members

RE: Good Friday Closing - Settlement Dates

Securities markets and the NASDAQ System will be closed on March 28 in observance of Good Friday (NASD Notice to members: 75-10, Schedule of Holidays). Transactions made on the business days immediately preceding that day will be subject to the schedule of settlement dates described below (for "regular-way" transactions).

March 28 shall not be considered as a business day for any purpose.

Schedule for "regular-way" transactions

<u>Trade Date</u>	<u>Settlement Date</u>
March 21	March 31
24	April 1
25	2
26	3
27	4
28 Good Friday	-
March 31	7

Questions regarding this notice may be directed to the Uniform Practice Division of National Clearing Corporation \*, 2 Broadway 8th Floor, New York, N.Y. 10004 -(212) 952-4018.

\* This notice, which applies to all NASD members, has been issued by National Clearing Corporation. The Board of Directors of NCC interprets and enforces the provisions of the NASD's Uniform Practice Code.

**NASD**

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.  
1735 K STREET NORTHWEST • WASHINGTON D. C. 20006

March 31, 1975

**I M P O R T A N T**

PROPOSED NEW ENTRY STANDARDS  
AND REQUIREMENTS FOR REGISTRATION  
OF PRINCIPALS AND REPRESENTATIVES

- TO: All NASD Members and Interested Persons
- RE: Proposed Amendments to Schedule C, Article 1,  
Section 2(d), of the By-Laws Concerning
- (a) Part I - Qualifications and Procedures for Being  
Admitted to Membership in the Association
  - (b) Part II - Registration of and Qualifications for Var-  
ious Categories of Principals and Representatives

Enclosed herewith are proposed amendments to Schedule C of the Association's By-Laws which concern qualification standards for membership in the Corporation and the requirements for registration with the Corporation of persons associated with a member, including requirements for qualification examinations to be given. These amendments have been proposed by the Board of Governors of the Association.

The proposed changes are being published at this time to enable all interested parties an opportunity to comment thereon. Such comments must be in writing and received by the Association by April 30, 1975 in order to receive consideration. After the comment period has expired, the proposals must again be reviewed by the Board. If the proposals, or an amended version thereof, are at that time approved by the Board, they must be submitted to and not disapproved by the Securities and Exchange Commission prior to becoming effective.

Explanation of Proposals

The proposed amendments to Schedule C which are enclosed herewith, and explained further below, represent a continuation of the Association's efforts to strengthen the adequacy of standards for entry into the

securities business and to develop meaningful qualifications criteria for those persons associated with a member who are required to register with the Corporation. In Notice to Members 73-63, dated September 14, 1973 (hereafter the 1973 proposals), the Board submitted for membership comment a variety of proposed amendments to Schedule C the provisions of which dealt with, among other things, qualifications and procedures for being admitted to membership including the concept of imposing restrictions upon a new member's business in a manner consistent with its demonstrated capabilities and expertise. Since substantial reference is made to the 1973 proposals, they should be reviewed in relation to the proposed amendments herein as well as to the existing provisions of Schedule C. The proposed amendments which are presented herein represent an extension of the ideas and concepts embodied in the earlier proposals, the comments received thereto, and the recommendations of several committees of the Board of Governors. They also represent a significant departure from the existing requirements for the registration of principals and representatives and should, therefore, be carefully studied by all members.

The proposed amendments to Schedule C incorporate a number of new areas and concepts of qualification at both the representative and principal levels of registration which heretofore have not been a part of the Association's qualification and registration requirements for associated persons. They would establish minimum qualification requirements for registered persons in terms of the intended area of business activity and job function in which such persons plan to engage. Thus, they would establish various categories of registration by specialization at both the principal and representative levels as follows:

#### Category of Principal Registration

1. General Securities Principal
2. Financial and Operations Principal
3. Underwriter Principal
4. Limited Principal - Investment Company and Variable Contracts Products
5. Limited Principal - Direct Participation Programs
6. Limited Principal - Options
7. Limited Principal - Securities Trading

#### Category of Representative Registration

1. General Securities Representative
2. Securities Trader Representative
3. Investment Company and Variable Contracts Products Representative
4. Direct Participation Programs Representative
5. Real Estate Securities Representative

A section-by-section analysis of the proposals commences on the following page. The Schedule C amendments are considered necessary and important by the Board of Governors and in the public interest; hence, it urges all members and interested persons to comment thereon.

All comments should be addressed to Mr. Donald H. Burns, Secretary, National Association of Securities Dealers, Inc., 1735 K Street, N.W., Washington, D.C. 20006 and should be received by April 30, 1975 in order to receive consideration. All communications will be considered available for inspection. Any questions concerning this notice should be directed to Mr. Jack Rosenfield at (202) 833-4828 or Mr. Frank J. McAuliffe at (202) 833-7394.

Sincerely,

A handwritten signature in cursive script, appearing to read "Frank J. Wilson".

Frank J. Wilson  
Senior Vice President  
Regulation

Explanation and Summary of the  
Proposed Amendments to Schedule C,  
Article 1, Section 2(d), of the By-Laws

Introductory Paragraph

The introductory paragraph merely explains that Schedule C is authorized by and adopted pursuant to Article 1, Section 2(d) of the By-Laws. The language of this paragraph is unchanged from the 1973 proposals.<sup>1/</sup>

Schedule C as proposed is divided into two parts. Part I concerns qualifications for membership for applicants as well as existing members and contains some provisions which appear in existing Schedule C commencing on page 1047 of the Association's Securities Dealers Manual. Proposed amendments concerning entry standards and pre-membership qualification requirements, among other things, have previously been submitted to the membership for comment<sup>2/</sup> and will not be republished at this time. They will, however, be submitted as part of completed Schedule C subsequently to be filed with the SEC for nondisapproval. It should be noted that certain very significant changes have been made to the 1973 proposals concerning, among other things, a new requirement that applicants for membership and existing members that are sole proprietorships shall have at least two persons at all times qualified and registered as principals. A waiver provision is still provided, however, enabling the President of the Corporation to waive the requirement as to applicants for membership and existing members in certain circumstances.

Proposed Part II also has significant new concepts in that it would establish new categories of registration for principals and representatives with each category to be determined by the area of business activity and/or job function in which such persons will engage for the member firm. This approach to registration (except for the Financial and Operations Principal category) is entirely new. In certain principal categories, prerequisites to registration as such are being proposed. As an aid to understanding the proposed new categories and qualifying prerequisites, the following outline provides first, the name of the new principal category, and second, the prerequisite category of representative registration in which a person would have to be qualified and registered. Successful completion of appropriate Qualification Examinations would, of course, be required before registration in any category could become effective.

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<sup>1/</sup> Notice to Members 73-63, dated September 14, 1973.

<sup>2/</sup> Ibid., pp. 29-35.

<u>Category of Principal Registration</u>	<u>Minimum Prerequisite Category of Representative Registration</u>
1. General Securities Principal	General Securities Representative
2. Financial and Operations Principal	No prior registration in any category required
3. Underwriter Principal	General Securities Representative
4. Limited Principal - Investment Company and Variable Contracts Products	Either General Securities Representative or Investment Company and Variable Contracts Products Representative
5. Limited Principal - Direct Participation Programs	Either General Securities Representative, Direct Participation Programs Representative or Real Estate Securities Representative
6. Limited Principal - Options	General Securities Representative
7. Limited Principal - Securities Trading	Either General Securities Representative or Securities Trader Representative

As stated above, the new categories of registration for representatives being proposed are:

1. General Securities Representative
2. Securities Trader Representative
3. Investment Company and Variable Contracts Products Representative
4. Direct Participation Programs Representative
5. Real Estate Securities Representative

A General Securities Representative registration would qualify a person to sell, solicit and otherwise engage in a full range of securities activities and products for a member while the limited categories of representative registration are proposed for those persons who intend to restrict their securities activities to a limited range of securities products. In this vein, a person registered as a representative in any category other than General Securities Representative could become registered, after qualifying for such, in a limited principal category without having to register as either a General Securities Representative or General Securities Principal so long as the limited principal category corresponds to the representative category by way of business activity and/or product mix; i. e. a Real Estate Securities Representative may qualify and register as a limited principal by passing only the appropriate Qualification Examination for Limited Principal - Direct Participation Programs. While separate categories of registration are being proposed at the representative level for

direct participation programs and real estate securities, respectively, the Board believes only one category of limited principal registration is necessary to satisfy the principal registration requirements for persons engaged in the solicitation and sale of such products. Therefore, any person registered solely as a Real Estate Securities Representative may qualify and register solely as a Limited Principal - Direct Participation Programs in order to function as a principal with respect to real estate securities.

Although the General Securities Principal category does encompass certain of the other limited principal categories, it does not qualify a person to function as a Financial and Operations Principal, Underwriter Principal or Limited Principal - Options. Persons desiring to register as such would have to separately qualify. In addition, registration as a General Securities Representative would be a proposed prerequisite for the category of General Securities Principal which, heretofore, has not been a requirement for persons seeking registration as a principal. This is a significant change to existing requirements and comment is specifically requested in respect thereto.

#### Part I - Qualification for Membership

##### Section 1 - Principals; Requirements for Applicants for Membership and Existing Members

Subsection (a) - This subsection would establish the requirement that all applicants for membership, including a sole proprietorship, would be required to have at least two persons who are qualified and registered as principals before the applicant firm would be admitted to membership and that such persons must meet the experience requirement of subsection (d). The substantive change to this paragraph from the 1973 proposals<sup>3/</sup>, as well as to subsection (b), is the absence of an automatic exemption provision for sole proprietorships from the requirement to have two principals. Currently, the provisions of existing Schedule C exempt applicants for membership that are sole proprietorships from the two principal requirement. The Board of Governors believes that the two principal requirement, without exception, is necessary and in the public interest to insure the viability of a broker/dealer which would otherwise have only one principal and, in addition, to protect the public with whom the firm is dealing. With two qualified principals, the possibility of a void because of illness, vacation or otherwise developing in the management, supervision and direction that a broker/dealer must have would be lessened. However, an exemptive provision from the two principal requirement would still be

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<sup>3/</sup> Ibid., p. 28.



available in proposed subsection (e) for those firms that can support the contention that the registration of only one principal would not be contrary to the public interest.

Because persons qualified and registered solely as a Financial and Operations Principal may function only in that capacity [Part II, Section 2(b)(5)] if an applicant for membership intends to register only two principals, one of them would be required to qualify and register as a Financial and Operations Principal unless the exemptive provisions of Part I, Section 2(d) hereof, applied to the applicant firm. He would also have to satisfy the experience requirements of subsection (d) which would not otherwise be required of a Financial and Operations Principal.

Subsection (b) - This subsection contains a substantive change from the 1973 proposals <sup>4/</sup> and existing Schedule C in that every existing member including sole proprietorships would, by a date to be determined after the effectiveness of these proposals, be required to have two persons registered as principals with the Corporation. It should again be noted that if there are only two principals registered, one of them would be required to also qualify and register as a Financial and Operations Principal unless the exemptive provisions of Part I, Section 2(d), apply.

Subsection (c) - This subsection is new and points up the necessity that members must have registered at all times at least the two principals required to be registered with the Corporation pursuant to the provisions of subsections (a) or (b). This paragraph proposes that upon the termination of registration of either one or both of the principals registered in compliance with subsections (a) or (b), the member must immediately, but in no event later than 90 days following such termination(s), cause to be registered with the Corporation two principals as required pursuant to subsections (a) and (b) so as to again be in compliance therewith. The Board believes such provisions are necessary to insure that the integrity and viability of the broker/dealer operations do not diminish as a result of the absence of any one of the required principals for a protracted period of time.

Subsection (d) - This provision would impose a three year experience requirement on the principals required by subsection (a). The three years' experience would have to have been obtained within the five year period preceding the application for membership and the person requesting registration with the applicant member would have to have functioned in a managerial or supervisory capacity during the three year period. This is similar to the 1973 proposals <sup>5/</sup> except that recognition is being provided for those firms planning to engage in specialized segments of

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4/ Id.

5/ Id.

the securities industry. In this connection, the modified proposal allows the three year experience requirement to be satisfied if such was in the industry related to the specialized field in which the firm plans to engage such as real estate or oil and gas direct participation programs relating to those industries.

In connection with the above, it may be necessary to refer to the earlier summarization of the various proposed categories of principal registration. In this regard, the question arises as to whether, under certain circumstances, the two principal requirement provided for in subsections (a) and (b) above should be allowed to be satisfied if such persons are registered only in a limited principal category or if, as the proposals now require, the two principal requirement is to be satisfied only by persons registered as General Securities Principals. The Board of Governors believes it is necessary and in the public interest for a general securities multi-product mix member firm to always have, at a minimum, two persons qualified and registered as General Securities Principals. However, the Board specifically invites comments with respect to whether, and under what circumstances, broker/dealers engaged only in specialized segments of the securities industry, such as mutual funds and tax sheltered programs, may satisfy the provisions of subsections (a) or (b) with persons qualified and registered solely in an appropriate limited principal category.

If the two principal requirement is to be satisfied with persons registered only in a limited principal category, the securities business and securities products in which such firms engage would necessarily be limited to only those activities permitted by the category of registration of the limited principals.

Subsection (e) - This subsection contains certain waiver provisions which would enable the President of the Corporation to:

- (1) waive the subsection (a) or (b) requirements for two principals upon written request and upon it being conclusively demonstrated that the public interest requires only one principal to be registered; and,
- (2) in exceptional cases, waive the subsection (d) three years' experience requirement upon written request of the individual and of the member with whom he is to be registered when the business background and experience of an individual justify that permitting registration of that individual would not be contrary to the public interest. The waiver of the experience requirement would not, however, per se, constitute a waiver of the requirement to take the appropriate Qualification Examination for principals.

Section 2 - Financial and Operations Principal; Requirements for Applicants for Membership and Existing Members

This section is essentially the same as the proposed Financial Principal requirements contained in the 1973 proposals<sup>6/</sup> with two important exceptions. First, the name of the category has been modified in recognition of the expanded coverage of operations matters to be included on the attendant Qualification Examination and, second, it proposes that persons designated as Financial and Operations Principals shall not be required to first qualify and register in any other category of representative or principal registration. The Board believes this category of registration bespeaks a function so peculiar to the securities industry as to warrant qualification and registration by examination only and not by any other prerequisite. A person qualified in another category of principal registration could, of course, become registered as a Financial and Operations Principal.

Section 3 - Underwriter Principal; Requirements for New Members and Existing Members

Provisions relating to Underwriter Principals for new and existing members engaging in investment banking activity (as defined therein) were submitted to the membership and interested persons for comment on March 14, 1973, as part of Notice to Members 73-17. Part I, Section 3, of proposed Schedule C contains provisions which would require new members and existing members who intend to engage in investment banking activity to designate at least one person as an Underwriter Principal who would be required to qualify and register as such before the member could engage in investment banking activity. In addition, certain definitions are also included in Part I, Section 3(c), in order to make clear the meaning of the words "investment banking activity," "selling group member," "new member" and "existing member" as they apply to the provisions relating to Underwriter Principals. Although such definitions are self-explanatory, it should be noted that in the definition of "selling group member," the phrase, ". . . securities being offered," shall mean the total number of shares actually sold at the time the offering has been completed.

Provisions relating to the qualification and registration requirements for persons designated as Underwriter Principals, including the requirement for a Qualification Examination to be taken, are contained in Part II, Section 2(c), of proposed Schedule C and are explained in the corresponding section below.

Section 4 - Pre-Membership Requirements

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<sup>6/</sup> Ibid., pp. 28-29.

Section 5 - District Committees and Board of Governors;  
Authority and Criteria for Determining Quali-  
fications for Membership; Hearing Procedures

Section 6 - Removal of Restrictions

[Sections 4, 5 and 6 have already been submitted for membership comment as part of the 1973 proposals<sup>7/</sup> and are not being republished at this time. It is anticipated that they will be incorporated into Schedule C with only slight nonsubstantive modifications, if any, and will be filed with the Securities and Exchange Commission for nondisapproval as part of new Schedule C upon final approval by the Corporation's Board of Governors.

Part II - Registration Requirements

Proposed Part II of Schedule C specifies the registration requirements for principals and representatives and provides for (1) the introduction of various new categories of registration at both the principal and representative levels and (2) the requirement that appropriate Qualification Examinations be taken and passed for each such category. The concept behind the creation of these new categories is a desire by the Board of Governors to define the Association's qualification and registration program in terms of (1) the job function to be performed and (2) the area of business activity in which persons requiring registration will engage for the member. Each category of limited registration establishes minimum qualification requirements for those applicants for registration intending to restrict their securities activities to a limited product mix. Thus, a person who intends to initiate a career in the securities industry limited solely to the sale of mutual funds would, as a minimum requirement, have to qualify and register only as an Investment Company and Variable Contracts Products Representative. On the other hand, a person desiring to engage in a general securities business would be required to qualify as a General Securities Representative. While the respective categories of limited registration appropriately limit the scope of the business activity in which such persons may engage, applicants for limited registration are provided with an alternative to the more comprehensive qualification procedures attendant to the General Securities Principal and General Securities Representative categories of registration. Registration in one or more categories of limited registration will not preclude such persons at a future date from qualifying for and registering in the most inclusive general securities category of registration. In addition, the proposals herein provide that a person registered solely in a limited representative category may qualify and register in the corresponding limited principal category by passing only

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<sup>7/</sup> Ibid., pp. 29-35.

the appropriate Qualification Examination without having to first qualify and register as either a General Securities Principal or General Securities Representative. A person desiring to engage in a limited scope of business activity may, if he so desires, qualify as a General Securities Representative by taking the appropriate Qualification Examination.

Appropriate grandfather provisions are included within Part II which allow persons registered before an as yet unspecified date as representatives and principals to qualify and register as a General Securities Representative and a General Securities Principal, respectively, without having to pass any Qualification Examination.

### Section 1 - Registration of Principals

Subsection (a) - This subsection delineates the requirement that persons who are to function in the capacity of "principals" must qualify and register with the Corporation in a principal category determined by the function they will perform with the member. It also specifies that a Qualification Examination appropriate to the category of registration intended shall be taken and passed before such registration can become effective. It should be noted that as part of the Board's proposal to adopt registration categories by specialization that Qualification Examinations tailored to the respective registration categories are being prepared.

Subsection (b) - This subsection contains the definition of principal which is unchanged from the 1973 proposals<sup>8/</sup>. It makes clear that anyone engaged in the management, direction or supervision of the day-to-day activities of a member's investment banking or securities business shall be registered as a principal. This section is not dissimilar from existing provisions in that it spells out certain specific categories of persons who would be required to be registered as principals including, among others, persons associated with a member engaged in training persons who are required to be registered as principals. Corporate directors and nominal officers would not be required to register as principals unless they were engaged in the management, direction or supervision of the day-to-day activities of the member's business.

Subsection (c) - This subsection is new and proposes that persons associated with a member who are responsible for training persons who are required to be registered with the Corporation as principals would themselves be required to register with the Corporation as either a General Securities Principal or as a principal in a category of registration comparable to those categories in which the persons they are training will be registered. The Board believes this proposal to be appropriate and believes

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<sup>8/</sup> Ibid., p. 35.

that persons engaged in training activities should have a level of qualification at least equal to that for which they are training others.

Subsection (d) - This subsection imposes the requirement that an appropriate Qualification Examination shall be required for persons whose most recent registration as a principal in the category for which he is filing an application has been terminated, or if he has ceased to function as such, for a period of two years or more immediately preceding the filing of such application. Thus, if a person previously registered as a General Securities Principal changes employers and thereafter for two years or more acted in the capacity of a limited principal, he would be required to pass the Qualification Examinations for General Securities Principal should he, subsequent to that two year period, again desire to function in such capacity. The same requirement would apply to the other principal categories.

The provisions of this subsection point up the necessity for all members to comply with the requirement that a person's current registration be consistent with the function being performed. In other words, if a principal was not currently performing the function of such, he should be reclassified and members would have the obligation of notifying the Corporation of such.

Subsection (e) - This subsection provides that the President of the Corporation, or his delegate, in exceptional cases where good cause is shown, may waive the requirement that an applicant for principal registration take and pass a Qualification Examination prior to his performing the function for which he is seeking registration. The language is substantially the same as in the 1973 proposals<sup>9/</sup> and is not dissimilar from existing provisions of Schedule C. It is important to note that this section requires that the application for a waiver be in writing and signed by a registered principal of the firm with whom the applicant is to be registered. It also makes clear that waivers will not routinely be granted; rather, they will be the exception rather than the rule.

Subsection (f) - Subsection (f) prescribes that a person registered as a representative whose duties are changed to that of a principal pass an appropriate Qualification Examination for the category of principal registration required as a result of his new function and satisfy other qualification prerequisites, if any. The provisions of this subsection are unchanged from the 1973 proposals.<sup>10/</sup>

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<sup>9/</sup> Ibid., pp. 46-47.

<sup>10/</sup> Ibid., p. 36.

Section 2 - Categories of Principal Registration

Subsection (a) - General Securities Principal

Subsection (a)(1) - This paragraph specifies the registration and qualification requirements for persons who are to function as General Securities Principals. While this category is essentially similar to the existing "principal" category, a new concept is being introduced which would require all future applicants who register as a General Securities Principal to first qualify and register as a General Securities Representative before the principal registration may become effective. Persons whose activities in the member's investment banking or securities business would encompass functions requiring registration only in one or more of the limited categories of principal registration would be permitted, at their discretion, to qualify and register as General Securities Principals. However, it should be noted that Part I, Sections 1(a) and 1(d) require that applicants for membership have two General Securities Principals registered with it each of whom is required to have at least three years' prior experience with a broker/dealer during the preceding five year period in a managerial capacity to qualify for membership.

Subsection (a)(2) - This paragraph provides for a general grandfather clause exempting all persons registered as a principal before an as yet unspecified date from the requirement to pass the Qualification Examination for General Securities Principal. Such persons would automatically be registered as a General Securities Principal subject to the provisions of Part II, Section 1(d) hereof relating to the requirement to take an appropriate Qualification Examination upon the lapse of registration for a two year period.

Subsection (a)(3) - This paragraph provides that any person registered solely as a General Securities Principal shall not be qualified to function as either a Financial and Operations Principal, Underwriter Principal or as a Limited Principal - Options unless also qualified and registered in each such category. However, the General Securities Principal category does encompass the limited principal categories of Investment Company and Variable Contracts Products, Securities Trading and Direct Participation Programs and, as such, separate qualification for and registration in those categories is not required. The Board believes that in order to effectively carry forward the concept of qualification and registration by job function and business activity, recognition must be given to those members of the Corporation and persons required to be registered specializing in a limited range of securities products and is of the opinion that to require such persons to spend the time, money and effort to qualify for areas in which they will have no contact would represent an unjust burden on such

persons. In this connection, the limited principal categories being proposed correspond by business activity to the proposed limited categories of representative registration. This concept would negate the requirement of having a representative dealing in a limited range of securities to qualify and register as a General Securities Principal in order for him to function as a principal.

However, the Board believes that the investment banking and securities business activities encompassing underwriting and options are sufficiently important and technical in nature so as to require separate qualification and registration for persons, including General Securities Principals, who will function as principals in those respective categories. Similar rationale applies to the category of Financial and Operations Principal.

Subsection (b) - Financial and Operations Principal - The provisions of this subsection are essentially the same as those contained in the 1973 proposals<sup>11/</sup> with two exceptions. First, the name of the category has been modified to Financial and Operations Principal in recognition of the expanded coverage of operations matters that are to be included in the Qualification Examination. The second one concerns the absence of any prerequisite that a person designated as a Financial and Operations Principal first qualify and register in any other category of principal or representative registration. Currently, every person registering as a Financial Principal is also required to qualify and register with the Corporation as a principal. Under the amended proposal, such persons would only be required to pass the appropriate Qualification Examination for Financial and Operations Principal in order to qualify and register as such.

The other provisions of this subsection define the term "Financial and Operations Principal," reference certain exemptions and provide that a person registered as such is qualified only to function as a Financial and Operations Principal and is not qualified to act in any other principal capacity. Therefore, as stated above, if a member has only two persons registered with it pursuant to Part I, Section 1 hereof, one of them would be required to qualify and register with the Corporation as a General Securities Principal and as a Financial and Operations Principal unless the exemptive provisions of Part I, Section 2(d) of Schedule C applied to the applicant firm.

Subsection (c) - Underwriter Principal - Provisions relating to the registration requirements for persons designated as an Underwriter Principal were previously submitted to the membership for comment on March

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<sup>11/</sup> Ibid., pp. 37-39.



13, 1973, as part of Notice to Members 73-17. The qualification and registration provisions contained herein remain essentially the same with only one substantive change being proposed. In this connection, the original proposal provided that persons designated as an Underwriter Principal were required to also register as a principal before their registration as an Underwriter Principal could become effective. Under the amended proposal, any person designated to qualify and register as an Underwriter Principal would not be required to qualify as a principal in any other category but would be required to qualify and register as a General Securities Representative, only, before his registration as an Underwriter Principal could become effective. Thus, while a person qualified and registered solely as an Underwriter Principal may not function in any other principal capacity, he may continue to function as a General Securities Representative. He could also qualify as a General Securities Principal if he so desired.

Subsection (d) - Limited Principal - Investment Company and Variable Contracts Products - The provisions of this subsection specify the qualification and registration requirements that must be fulfilled in order for a person to be registered in the category of Limited Principal - Investment Company and Variable Contracts Products. This category of principal registration would be available to those persons who would function as a principal with such responsibility limited to securities of companies registered pursuant to the Investment Company Act of 1940 and variable contracts products and insurance premium funding programs registered pursuant to the Securities Act of 1933 and include the following:

- (1) open end investment company shares;
- (2) closed end investment company shares only in the initial issue;
- (3) face amount certificates;
- (4) unit investment trusts;
- (5) variable contracts; and,
- (6) insurance premium funding programs.

In order to qualify and register as a Limited Principal - Investment Company and Variable Contracts Products, a person would be required by this section to qualify and register as either a General Securities Representative or as an Investment Company and Variable Contracts Products Representative and to pass the Corporation's appropriate Quali-

fication Examination for Limited Principal - Investment Company and Variable Contracts Products before such registration could become effective.

Any person registered solely as a Limited Principal - Investment Company and Variable Contracts Products would not be qualified to function as, or act in the capacity of, a General Securities Principal, Financial and Operations Principal, Underwriter Principal, Limited Principal - Options, or any other category of limited principal unless also qualified and registered in each such category of registration. Thus, while a Limited Principal - Investment Company and Variable Contracts Products, previously registered as a General Securities Representative, could engage in the solicitation and sale of securities generally, the managerial and supervisory responsibilities attendant to his limited principal classification would be restricted to only those securities products provided for in Part II, Section 2(d) of Schedule C.

Subsection (e) - Limited Principal - Direct Participation Programs - The provisions of this subsection specify the qualification and registration requirements for a person to qualify and register in the category Limited Principal - Direct Participation Programs. This level of principal registration would thus be available only to those persons who would function as a principal with responsibility over the limited and specific range of securities products referred to as direct participation programs, including real estate securities.

Thus, the activities in which a Limited Principal - Direct Participation Programs could engage as a principal would be limited to direct participation programs as defined in Part II, Section 2(e) of Schedule C.

In order to qualify and register as a Limited Principal - Direct Participation Programs, a person would be required to qualify and register as a General Securities Representative, a Direct Participation Programs Representative, or as a Real Estate Securities Representative and pass the appropriate Qualification Examination before such registration could become effective.

Subsection (e)(2) specifies that any person registered solely as a Limited Principal - Direct Participation Programs would not be qualified to function as, or act in the capacity of, a General Securities Principal, Financial and Operations Principal, Underwriter Principal, Limited Principal - Options, or another category of limited principal unless he was also qualified and registered in each such category of registration.

Subsection (e)(3) defines the words "direct participation programs" and specifies the securities products included in such and is self-explanatory.

Subsection (f) - Limited Principal - Options - The provisions of this subsection specify the qualification and registration requirements that would have to be fulfilled in order for a person to qualify and register in the category Limited Principal - Options. This category of registration is required of those persons whose activities will be limited to the solicitation, sale, endorsement and/or writing of options for the member.

In order to qualify and register as a Limited Principal - Options, a person would be required to qualify and register as a General Securities Representative and pass the appropriate Qualification Examination for Limited Principal - Options before such registration could become effective. It is important to note that a person registered solely as a General Securities Principal would not be qualified to function as a Limited Principal - Options. He would first be required to pass the appropriate Qualification Examination for Limited Principal - Options before he could function as such with a member whose securities business includes the solicitation, sale, endorsement and/or writing of options. The Board believes this requirement is essential in view of the significantly different nature of the options business from that of the general securities business. It also believes this requirement is necessary because of the current (and probably future) popularity of options as well as the possibility of publishing over-the-counter options quotations on NASDAQ if studies presently underway determine such to be feasible.

Subsection (g) - Limited Principal - Securities Trading - The provisions of this subsection specify the qualification and registration requirements that would have to be fulfilled in order for a person to qualify and register as a Limited Principal - Securities Trading. This level of registration would be available to those persons who would function as a principal and whose activities would be limited solely to exercising discretionary authority in trading securities and/or effecting market making securities transactions in the over-the-counter securities market for or on behalf of the member.

In order to qualify and register as a Limited Principal - Securities Trading, a person would be required by subsection (g)(1) to qualify and register as either a General Securities Representative or as a Securities Trader Representative and to pass the appropriate Qualification Examination for Limited Principal - Securities Trading before such registration could become effective.

Any person registered solely as a Limited Principal - Securities Trading would not be qualified to function as, or act in the capacity of, a General Securities Principal, Financial and Operations Principal, Underwriter Principal, Limited Principal - Options, or another category of

limited principal unless also qualified and registered in each such category of registration. In addition, any person registered solely as a Limited Principal - Securities Trading who was previously registered only as a Securities Trader Representative would not be qualified to solicit, sell and/or otherwise personally service accounts of public customers nor function as a principal with responsibility over persons who are so qualified and registered.

### Section 3 - Registration of Representatives

Subsection (a) - This subsection delineates the requirement that persons who are to function as "registered representatives" must register with the Corporation in the category of representative as determined by the function such persons will perform with the member. In addition, a Qualification Examination appropriate to the category of registration would be required to be passed before such registration could become effective. As stated above, this concept of registration by specialization is new. The Board feels such is appropriate in view of the changing nature of the securities business and in view of the increased emphasis on specialization in certain segments thereof.

Subsection (b) - This subsection defines the term representative and, except for some minor nonsubstantive language changes, is the same as that contained in the 1973 proposals<sup>12/</sup> and is not dissimilar from that contained in existing Schedule C. Proposed subsection (b) contains a new requirement that a person responsible for the member's compliance with securities industry regulations would be required to qualify and register as a registered representative if not otherwise required to register as a principal. This new provision would make certain that those persons designated by a member as having supervisory responsibilities for the firm's compliance with appropriate rules and regulations covering the conduct of its investment banking or securities business would fall within the definition of the term "registered representative" if not otherwise required to be registered as principals.

The significance of the provisions relating to persons engaged in compliance activities for members is that presently many such persons are not registered. After effectiveness of these proposals, registration of such persons would be required. It should be made clear, however, that this does not mean the ultimate responsibility for supervision of such is transferred in any way from those engaged in the management of the member's investment banking or securities business. In this connection, it is well established by case law and decisions of the SEC that ultimate responsibility for such is always in management.

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<sup>12/</sup> Ibid., pp. 39-40.

The Board of Governors believes that, conceptually, supervisory persons and persons responsible for the member's compliance with securities industry rules and regulations should be qualified and registered as principals. Nevertheless, the Board is also cognizant of the various levels of supervisory responsibility which exist within the Association's heterogeneous membership and the registration implications of requiring all such persons to qualify and register as principals. The Board specifically requests comments with respect to whether, and under what circumstances, persons who function with supervisory responsibility and with responsibility for compliance matters should qualify and register with the Corporation in a principal level of registration.

Subsection (c) - This subsection is new and provides that persons associated with a member engaged in training activities, unless otherwise required to be registered as principals, would have to qualify and register with the Corporation in a category of representative registration comparable to that for which they are training others. Therefore, persons responsible for the training of persons associated with a member for registration as General Securities Representatives would themselves be required to qualify and register in that category if not otherwise required to be registered as a principal. The Board believes this proposal to be appropriate because it believes persons engaged in training activities should have a level of qualification at least equal to that for which they are training others.

Subsection (d) - This subsection would impose the requirement that an appropriate Qualification Examination would be required for any person whose most recent registration as a representative has been terminated for a period of two years or more immediately preceding the filing of a new application unless such person has been continuously registered with the Corporation as a principal. This is comparable to provisions of existing Schedule C and the 1973 proposals.<sup>13/</sup>

Subsection (e) - This subsection provides that the President of the Corporation, or his delegate, may waive the requirement that an applicant for representative registration take and pass a Qualification Examination prior to his performing the function for which he is seeking registration. The language is substantially the same as in the 1973 proposals<sup>14/</sup> and is comparable to provisions in existing Schedule C.

Subsection (f) - Grandfather Clause - This paragraph contains a general grandfather clause and provides that all persons registered as representatives before September 1, 1974, would be automatically registered as General Securities Representatives and would not be required to pass

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<sup>13/</sup> Ibid., p. 40.

<sup>14/</sup> Ibid., p. 46.

any Qualification Examination, subject to the provisions of subsection (d) above. In addition, provision is made for those persons whose applications for registration were on file with the Corporation before September 1, 1974, and who subsequent to that date pass an appropriate Qualification Examination to be registered as General Securities Representatives. In Notice to Members 74-34, dated August 10, 1974, the membership was advised that after September 1, 1974, all applications for registration as representatives must indicate whether the applicant was applying for registration as a General Securities Representative or as a representative in a limited category of registration. In addition, the notice explained that a new and more encompassing Qualification Examination would be administered after September 1, 1974 and required for a person to qualify and register as a General Securities Representative. For those persons intending to register in one or more of the limited categories, the existing registered representative examination only would be required until such time as specialized Qualification Examinations were established for each of the limited representative categories of registration.

Therefore, the effect of this proposed grandfather clause would be to qualify and register persons whose applications for registration were on file before September 1, 1974, and would otherwise be allowed to qualify and become registered as a General Securities Representative by taking the then existing Qualification Examination. However, such applicants have only until March 31, 1975, to take and pass this examination in order to so qualify as explained in a later Notice to Members 75-20, dated February 28, 1975. This notice explains that as of April 1, 1975, individuals whose applications were on file prior to September 1, 1974, who wish to register as a General Securities Representative will be required to take and pass the more comprehensive Qualification Examination for General Securities Representative in order to qualify and register as such.

#### Section 4 - Categories of Registration of Representatives

This section embodies a new concept in the registration of representatives in that it proposes a system of categories of registration by specialization in addition to providing a broad all inclusive category of registration for those who do not desire to limit their selling activities or are otherwise required to register as such because of the generally broad nature of their activities in the investment banking or securities business. Thus, while all persons who intend to initiate a career in the investment banking or securities business limited solely to the sale of mutual funds or variable contracts would have only to qualify and register in the limited category of registration of Investment Company and Variable Contracts Products Repre-

sentative, they would still have the option of qualifying for and registering in the all inclusive category of General Securities Representative. Persons intending to register only in a limited category of representative registration are advised to study first the qualification and registration requirements for the various proposed categories of principal registration so that, should they later desire to function as a principal, their intended category of representative registration is the appropriate prerequisite for that particular principal category of registration.

Subsection (a) - General Securities Representative - Initially, this subsection specifies the qualification and registration requirements for persons who are to function as representatives with a member whose activities will include, but not necessarily be limited to, the solicitation or sale of securities generally or whose duties are covered by more than one of the other registration categories embodied in Section 4. A person registered in this category would have no restrictions on the types of securities he could sell or the type of activity he could engage in at the representative level.

In addition, persons having supervisory responsibility for a member's compliance with the rules and regulations of the Corporation, the Securities and Exchange Commission and all applicable federal securities laws would also be required to register with the Corporation as a General Securities Representative if not otherwise required to register as a principal. As stated above, the significance of this proposed requirement is that presently many such persons engaged in compliance activities for members are not qualified or registered as either representatives or principals. After effectiveness of these proposals, registration of such persons would be required.

Any person required to register with the Corporation as a General Securities Representative would be required to pass an appropriate Qualification Examination before such registration could become effective.

Persons whose activities in the member's investment banking or securities business would encompass functions requiring registration only in one or more of the categories of limited representative registration would be permitted, at their discretion, to qualify and register as General Securities Representatives. However, it should be noted that registration as a General Securities Representative is required for those persons desiring to register as a (1) General Securities Principal, (2) Underwriter Principal or (3) Limited Principal - Options and, as such, initial registration as a General Securities Representative may be appropriate for many persons who would not otherwise be required to register as such at the outset.

Subsection (b) - Securities Trader Representative - The provisions of this subsection specify the qualification and registration requirements for a person who is required to register with the Corporation as a representative in the category Securities Trader Representative. This would be a new category of representative not presently provided for in Schedule C.

A person electing to qualify and register in this category of registration would be required to pass an appropriate Qualification Examination before such registration could become effective. This level of registration is available to those persons whose activities as a representative involve exercising discretionary authority in trading securities and/or effecting market making securities transactions in the over-the-counter securities markets for or on behalf of the member if such persons are not otherwise required to be registered as principals.

A person registered solely as a Securities Trader Representative may not solicit, sell and/or otherwise personally service accounts of public customers unless he is also registered as a General Securities Representative, Investment Company and Variable Contracts Products Representative, Direct Participation Programs Representative, or as a Real Estate Securities Representative and as long as his retail activities are not inconsistent with the category of registration.

This section would obviate the need for full registration for a person who engages only in trading activities as is now the case. It would also make clearer than existing provisions those persons engaged in order room or trading activities who would be required to be registered. In this regard, the provisions relating to this category of registration specify that registration as a Securities Trader Representative would be required of all persons who exercise discretionary authority while effecting market making transactions or while trading securities for the member. The emphasis, as such, on the existence of discretionary authority makes clear the need for members to carefully supervise persons involved in order room activities to make certain that clerical assistants and others who customarily assist in such activities do not exercise such authority and thereby function in a capacity that would require their registration as a Securities Trader Representative.

Subsection (c) - Investment Company and Variable Contracts Products Representative - The provisions of this subsection specify the qualification and registration requirements that must be fulfilled for representatives whose activities would be limited to the sale of securities of companies registered pursuant to the Investment Company Act of 1940, variable contracts products and insurance premium funding programs registered pursuant to the Securities Act of 1933.



Any person electing to qualify and register in this category of registration would be required to pass an appropriate Qualification Examination before such registration may become effective. A person registered solely as an Investment Company and Variable Contracts Products Representative would not be qualified to engage in the solicitation and sale of securities generally and would be required to restrict his activities only to those securities products specified in subsection (c). If he desired to broaden his activities to any other securities product, he would have to first become registered in the category or registration appropriate to his contemplated activities.

A category of registration such as this has long been sought by the investment company and insurance segments of the securities industry and the Board believes providing such a category will materially assist broker/dealers in those segments of the industry in that their prospective representatives will no longer be required to be trained in areas in which they will conduct no business.

Subsection (d) - Direct Participation Programs Representative - The provisions of this subsection specify the qualification and registration requirements that must be fulfilled for a person to be registered as a representative in this new category of registration, Direct Participation Programs Representative. This category of registration would be available to those persons whose activities are to be limited to direct participation programs and real estate securities as defined in Part II, Sections 2(d) and 4(e), of Schedule C. Persons in this segment of the securities business have urged such a category of registration as they are, generally, not interested in selling a general line of securities; hence, the additional training and study required to qualify as a General Securities Representative, as is required under existing Schedule C, represents an unnecessary burden in terms of the time required and financial considerations involved in such training.

Subsection (e) - Real Estate Securities Representative - This also is a new category of representative. The provisions of this subsection specify the qualification and registration requirements to be fulfilled for a person to qualify and register as a Real Estate Securities Representative. This category of registration is available to those persons who desire to limit their sales activities to real estate securities as specified in the definition of Real Estate Securities Representative.

Any person electing to qualify and register in this category of registration would be required to pass an appropriate Qualification Examination before such registration may become effective. A person regis-

tered solely as a Real Estate Securities Representative would not be qualified to engage in the solicitation or sale of any other securities. The real estate segment of the securities industry has urged a category of registration such as this and the Board believes it is appropriate.

Section 5 - Special Situations

Section 6 - Persons Exempt From Registration

Section 7 - Qualification Examinations and Procedures

[Section 5 contains special registration situations involving foreign associates and persons associated with SECO members. Section 6 specifies those persons who are not required to be registered with the Corporation. Section 7 relates to the procedures for taking the Corporation's Qualification Examinations. These sections are essentially the same as contained in the 1973 proposals<sup>15/</sup> and are not dissimilar from provisions contained in existing Schedule C except for some nonsubstantive language changes and the relocation of certain paragraphs within these sections to improve the readability and presentation thereof.]

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<sup>15/</sup> Ibid., pp. 40-47.

PROPOSED NEW SCHEDULE C

(Page 1047 of the Manual)

It is proposed that existing Schedule C, adopted pursuant to Article I, Section 2(d) of the By-Laws of the Association, be withdrawn and the following Schedule C substituted in place thereof.

SCHEDULE C

This Schedule C has been prepared pursuant to the provisions of Section 2(d) of Article I of these By-Laws and contains qualification standards for membership in the Corporation and the requirements for registration with the Corporation of persons associated with a member, including requirements for qualification examinations to be given. Where applicable, compliance with the provisions of both Parts I and II of this Schedule must be satisfied before registration with, admission to or continuance in membership in the Corporation will be approved.

Part I - Qualification for Membership

Section 1 - Principals; Requirements for Applicants for Membership and Existing Members

(a) An applicant for membership in the Corporation shall have at least two persons associated with it who are qualified and registered as General Securities Principals pursuant to the provisions of Part II, Section 2(a) hereof, before it shall be admitted to membership. After admission to membership, a member shall continue at all times to have at least two persons associated with it who are qualified and registered as General Securities Principals.

(b) Every member of the Corporation shall, by \_\_\_\_\_, have at least two persons associated with it who are registered as General Securities Principals pursuant to the provisions of Part II, Section 2(a) hereof.

(c) In the event of termination of a person associated with a member registered with the Corporation as a principal pursuant to subsection (a) or (b), the member shall immediately, but in no event later than 90 days following the date of termination, cause to be registered with the Corporation two principals required by subsections (a) and (b) so as to remain in compliance therewith.

(d) Each principal required by subsection (a) hereof, shall have at least three years' prior experience with a broker/dealer within the preceding five year period from the date of application for membership and shall have functioned with such broker/dealer in a managerial or supervisory capacity during such three year period. With respect to applicant broker/dealers planning to engage in specialized segments of the securities industry such as real estate or oil and gas direct participation programs, the three year experience requirement will be satisfied if such was in the industry related to the specialized field in which the firm plans to engage in business.

(e) In an exceptional case when the business background and experience of an individual justifies that such would not be contrary to the public interest, the experience requirement imposed by subsection (d) hereof may, upon written request of the individual and of the member with whom he is to be registered, be waived by the President of the Corporation.

Notwithstanding the provisions of subsections (a) and (b) hereof, the President of the Corporation in situations which indicate conclusively that the public interest requires only one person associated with a member to be registered as a principal may, upon written request of the member, waive the requirements thereof.

Section 2 - Financial and Operations Principal; Requirements for Applicants for Membership and Existing Members

(a) Every applicant for membership who has not, pursuant to the provisions of subsection (d) hereof, been granted an exemption from such shall register with the Corporation one or more persons associated with it, one of whom shall be the firm's chief financial officer, as a Financial and Operations Principal pursuant to the provisions of Part II, Section 2(b) hereof before it will be admitted to membership in the Corporation.

(b) After an applicant has been admitted to membership, it must continue to have at least one registered Financial and Operations Principal, including the firm's chief financial officer, performing the duties of such who has satisfied the requirements of Part II, Section 2(b) hereof.

(c) Every member of the Corporation who has not, pursuant to the provisions of subsection (d) hereof, been granted an exemption from such shall, by \_\_\_\_\_, designate as a Financial and Operations Principal those persons associated with it, at least one of whom shall be the firm's chief financial officer, who perform the functions of such as specified in Part II, Section 2(b)(2) hereof. They shall be registered pursuant to the provisions of Part II, Section 2(b) hereof.

(d) A member, or an applicant for membership in the Corporation, may, upon written request, be exempted by the President of the Corporation from the requirement to have a Financial and Operations Principal if:

- (1) it has been expressly exempted by the Securities and Exchange Commission from SEC Rule 15c3-1 pursuant to the provisions of paragraph (b)(3) thereof; or,
- (2) it is subject to the provisions of SEC Rule 15c3-1(a)(3) and (4).

Section 3 - Underwriter Principal; Requirements for New Members and Existing Members

(a) New Members

- (1) Effective \_\_\_\_\_, every applicant for membership who intends to engage in investment banking activity shall designate with the Corporation at least one person as an Underwriter Principal the duties of whom shall include, but not necessarily be limited to, the organization and/or supervision of any participation in the origination or distribution of offerings of securities by the member whether as an underwriter or selling group member.
- (2) Before a new member may engage in investment banking activity, the designated Underwriter Principal shall qualify and register as such pursuant to the provisions of Part II, Section 2(c) hereof.

(b) Existing Members

- (1) Every member of the Corporation engaged in investment banking activity shall as of \_\_\_\_\_, designate at least one person as an Underwriter Principal whose duties shall include, but not necessarily be limited to, the organization and/or supervision of any participation in the origination or distribution of offerings of securities by the member whether as an underwriter or selling group member. The designated Underwriter Principal shall be required to qualify and register as such pursuant to the provisions of Part II, Section 2(c) hereof.

(c) Definitions - For the purposes of this Schedule C, the following words shall have the stated meanings:

- (1) "Investment Banking Activity" - shall mean the business carried on by a member of the Corporation of underwriting or distributing issues of securities, of purchasing securities and offering the same for sale as a dealer thereof, or of rendering financial and consulting assistance in the preparation and registration thereof.

- (2) "Selling Group Member" - shall mean a member of the Corporation engaged in a distribution of an offering of securities which distribution amounts to 10 per centum or more of the securities being offered.
- (3) "New Member" - shall mean a broker/dealer admitted to membership in the Corporation after \_\_\_\_\_, and/or which has been actively engaged in the investment banking and/or securities business for a period of less than one (1) year immediately preceding the filing of an application for Underwriter Principal.
- (4) "Existing Member" - shall mean a broker/dealer admitted to membership in the Corporation prior to \_\_\_\_\_, and which has been actively engaged in the investment banking and/or securities business for a period of not less than one (1) year immediately preceding the filing of an application for Underwriter Principal.

Section 4 - Pre-Membership Requirements

Section 5 - District Committees and Board of Governors; Authority and Criteria for Determining Qualifications for Membership; Hearing Procedures

Section 6 - Removal of Restrictions

[ Section 4 contains provisions relating to pre-membership requirements at the staff level, always in the appropriate District of the Association where the applicant for membership will have its principal place of business. Section 5 relates to procedures before either the District Committee or the Board of Governors in those situations where an applicant for membership is dissatisfied with the staff determination provided for in Section 4. Section 6 establishes the procedures for the removal of restrictions as to a member if the reasons for the restrictions having been imposed in the first place no longer exist. These sections have already been published for comment in the 1973 proposals. They are not, therefore, being republished at this time. It is anticipated they will be incorporated into Schedule C with only slight nonsubstantive modifications, if any, and will be filed as part of Schedule C with the Securities and Exchange Commission for nondisapproval upon final approval by the Board of Governors of new Schedule C. ]

Part II - Registration Requirements

Section 1 - Registration of Principals

(a) Registration Requirements - All persons associated with a member who are to function as principals shall be registered as such with the Corporation in the category of registration appropriate to the function to be performed as specified in Section 2 hereof. Before their registration can become effective, they shall pass a Qualification Examination for Principals appropriate to the category of registration as specified by the Board of Governors.

(b) Definition of Principal - The term "principal" shall mean a person associated with a member who is actively engaged in the management, direction or supervision of the day-to-day activities of the member's investment banking or securities business. Such shall include, but not necessarily be limited to:

- (1) sole proprietors;
- (2) corporate officers and directors who manage, direct or supervise the day-to-day investment banking or securities business of the member;
- (3) partners;
- (4) managers of Offices of Supervisory Jurisdiction; and,
- (5) persons engaged in and responsible for the training of persons associated with a member who are required to be registered with the Corporation as principals.

(c) Registration of Persons Engaged in Training - All persons associated with a member engaged in the training of persons whose activities in the investment banking or securities business encompass functions which require registration in one or more of the categories described in Sections 2(a) through 2(g) hereof, shall be required to qualify and register as a General Securities Principal or in another category of principal registration at least equivalent to that for which they are training such persons.

(d) Requirements for Examination on Lapse of Registration - Any person whose most recent registration as a principal in the category for which he is seeking registration has been terminated for a period of two or more years immediately preceding the filing of a new application for registration as a principal, or who has ceased to function as such for that period, shall be required to pass a Qualification Examination for Principals appropriate to the category of registration as specified by the Board of Governors before a new registration may become effective.

(e) Waiver of Requirement to Take Qualification Examination - In exceptional cases and where good cause is shown, the President of the Corporation, or his delegate, upon request by the member, may waive the requirement to take a Qualification Examination. All such requests shall be in writing, addressed to the President of the Corporation and signed by a registered principal of the requesting firm. Advanced age, physical infirmity, or experience in fields ancillary to the investment banking or securities business will not individually of themselves constitute sufficient grounds to waive the requirement to take a Qualification Examination. A request for a waiver based only upon the expiration of the two year period since the most recent registration with the Association will not be honored. Extensions of time beyond that specified within this Schedule will not be granted. Except where otherwise specified herein, Qualification Examinations required hereby shall be taken and passed by the applicant and the member shall receive notification of such from the NASD prior to the performance by the applicant of the functions for which he is seeking registration.

(f) Elevation to Principal Status - Any person associated with a member as a registered representative whose duties are changed so as to require any principal classification shall, within ten (10) business days thereof, submit a principal elevation form\* designated by the Board of Governors with the applicable examination fee. The applicant, assuming all prerequisites to the proposed category of registration have been met, shall be allowed a period of 90 calendar days following the change in his duties during which to pass the appropriate Qualification Examination for Principals. If the applicant fails the examination, the elevation form and application will be retained for an additional period of 90 calendar days from the date of the last failure. If the applicant fails to take the examination within the initial 90 calendar day period, a new principal elevation form and examination fee shall be required. In no event may such person function as a principal beyond the initial 90 calendar day period following the change in his duties without having successfully passed the appropriate Qualification Examination. In no event may a person previously unregistered in any capacity applying for principal status function as a principal until fully qualified.

## Section 2 - Categories of Principal Registration

### (a) General Securities Principal

- (1) All persons associated with a member who are included within the scope of Part II, Section 1 hereof, shall be required to register with the Corporation as a General Securities Principal and shall pass an appropriate Qualification Examination before such registration may become effective unless their activities are so limited as to qualify them for one or more of the limited categories of principal registration specified hereafter. Persons whose activities in the investment

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\*The form currently designated for this purpose is PE-3.



banking or securities business are so limited may, at their discretion, elect to become registered as a General Securities Principal. Any person required to register and qualify as a General Securities Principal subsequent to \_\_\_\_\_, must, prior to or concurrent with such registration, become registered pursuant to the provisions of Section 4(a) hereof, as a General Securities Representative.

- (2) Grandfather Clause - Any person who was registered with the Corporation as a principal on or before \_\_\_\_\_ and was designated as a sole proprietor, officer, partner, manager of Office of Supervisory Jurisdiction or director shall not be required to pass a Qualification Examination for General Securities Principal and, except as provided in Part II, Section 1(d) hereof, shall be qualified to be and shall be, registered with the Corporation as a General Securities Principal.
- (3) A person registered solely as a General Securities Principal shall not be qualified to function as either a Financial and Operations Principal, an Underwriter Principal or a Limited Principal - Options unless he is also qualified and registered as such pursuant to the provisions of subsections (b), (c) or (f) hereof, respectively.

(b) Financial and Operations Principal

- (1) All persons associated with a member not exempted by Part I, Section 2(d) from the requirement to have a Financial and Operations Principal who are to perform the duties of a Financial and Operations Principal shall be required to register as such with the Corporation and shall pass an appropriate Qualification Examination before such registration may become effective.
- (2) Definition of Financial and Operations Principal - The term "financial and operations principal" shall mean a person associated with a member whose duties include, but are not necessarily limited to:
  - a. final approval and responsibility for the accuracy of financial reports submitted to any duly established securities industry regulatory body;
  - b. final preparation of such reports;
  - c. supervision of individuals who assist in the preparation of such reports;
  - d. supervision of and responsibility for individuals who are involved in the actual maintenance of the firm's books and records from which such reports are derived;

- e. supervision and/or performance of the member's responsibilities under all financial responsibility rules promulgated pursuant to the provisions of the Securities Exchange Act of 1934; and,
  - f. overall supervision of and responsibility for the individuals who are involved in the administration and maintenance of the firm's back office operations.
- (3) Examination Requirement for Financial and Operations Principal of Existing Members - Except as provided in paragraph (4) hereof, any person required by the provisions of Part I, Section 2(c) hereof, to be designated as a Financial and Operations Principal must pass within 90 calendar days of the date of designation as such an appropriate Qualification Examination before such registration shall become effective.
- (4) Exemption From Requirement to Take Financial and Operations Principal Examination - Principals designated pursuant to the provisions of Part I, Section 2(c) hereof, shall not be required to take the Financial and Operations Principal Qualification Examination if:
- a. such person had been performing a Financial and Operations Principal function as defined in subsection (2) hereof, on or before September 1, 1972, with the member requesting this registration; and,
  - b. such person is named on an appropriate form\* designated by the Board of Governors which shall be filed with the Corporation no later than the close of business \_\_\_\_\_.
- (5) Persons registered solely as a Financial and Operations Principal shall not be qualified to function in a principal capacity with responsibility over any area of business activity not prescribed in this subsection (b).
- (c) Underwriter Principal
- (1) New Members
- a. Each person required by Part I, Section 3 hereof, to be designated as an Underwriter Principal shall have three years of experience with a member actively engaged in the origination

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\* The form currently designated for this purpose is Form MD-1.

of the underwriting of offerings of securities and shall demonstrate that a significant part of such person's business experience with the member entailed involvement in the organization and/or supervision of such broker/dealer's investment banking activity in order to register with a new member as an Underwriter Principal. In an exceptional case, when the business background and experience of the designated individual justifies such, the three year experience requirement imposed herein may be waived by the President of the Corporation upon written request of the designated person and the new member firm. In all such cases, the burden of justification for such waiver shall be upon the designated person.

- b. Each person required by Part I, Section 3 hereof, to be designated as an Underwriter Principal shall, as a prerequisite thereto, be registered as a General Securities Representative pursuant to the provisions of Section 4(a) hereof, and shall pass the appropriate Qualification Examination for Underwriter Principal and be registered as such before a new member in the Corporation may engage in investment banking activity. If the person designated as an Underwriter Principal is qualified and registered as a General Securities Representative pursuant to Section 4(a) hereof, such individual shall be required to pass only the Qualification Examination for Underwriter Principal.

(2) Existing Members

- a. Each person required by Part I, Section 3 hereof, to be designated as an Underwriter Principal shall have three years of experience with a member actively engaged in the origination of the underwriting of offerings of securities and shall demonstrate that a significant part of such experience entailed involvement in the organization and/or supervision of such broker/dealer's investment banking activity. In an exception case, when the business background and experience of the designated person justifies such, the three year experience requirement imposed herein may be waived by the President of the Corporation upon written request of the designated person and member firm.
- b. Each person required by Part I, Section 3 hereof, to be designated as an Underwriter Principal shall, as a prerequisite thereto, be registered as a General Securities Representative pursuant to the provisions of Section 4(a) hereof, and shall pass the Qualification Examination for Underwriter Principal and be registered as such before engaging in the organization and/or supervision of the member's investment banking activity.

c. Grandfather Clause - Any person designated as an Underwriter Principal who has been registered with a member or members as a principal for a period of at least three years prior to \_\_\_\_\_ and was actively engaged in the organization and/or supervision of the member's investment banking activity shall not be required to take any Qualification Examination in order to qualify and register as an Underwriter Principal, subject to the provisions of Part II, Section 1(d) hereof.

(3) Persons registered solely as an Underwriter Principal shall not be qualified to function in a principal capacity with responsibility over any area of business activity not prescribed in this subsection (c).

(d) Limited Principal - Investment Company and Variable Contracts Products

(1) All persons associated with a member who are included within the scope of Part II, Section 1 hereof, may register with the Corporation as a Limited Principal - Investment Company and Variable Contracts Products if:

- a. their activities in the investment banking and securities business are limited solely to securities of companies registered pursuant to the Investment Company Act of 1940 and variable contracts products and insurance premium funding programs registered pursuant to the Securities Act of 1933;
- b. they are currently qualified and registered as either a General Securities Representative or as an Investment Company and Variable Contracts Products Representative; and,
- c. they pass the appropriate Qualification Examination for Limited Principal - Investment Company and Variable Contracts Products.

(2) Persons registered solely as a Limited Principal - Investment Company and Variable Contracts Products shall not be qualified to function in a principal capacity with responsibility over any area of business activity not prescribed in this subsection (d).

(e) Limited Principal - Direct Participation Programs

(1) All persons associated with a member who are included within the scope of Part II, Section 1 hereof, may register with the Corporation as a Limited Principal - Direct Participation Programs if:

- a. their activities in the investment banking and securities business are limited solely to Direct Participation Programs as defined in paragraph (3) hereof;

- b. they are currently qualified and registered as a General Securities Representative, a Direct Participation Programs Representative or as a Real Estate Securities Representative; and,
  - c. they pass the appropriate Qualification Examination for Limited Principal - Direct Participation Programs.
- (2) Persons registered solely as a Limited Principal - Direct Participation Programs shall not be qualified to function in a principal capacity with responsibility over any area of business activity not prescribed in this subsection (e).
- (3) Definition of Direct Participation Programs - For purposes of this Schedule C, "direct participation programs" shall mean programs which provide for flow-through tax consequences regardless of the structure of the legal entity or vehicle for distribution including, but not limited to, oil and gas programs, real estate programs, agricultural programs, cattle programs, condominium securities, Subchapter S corporate offerings and all other programs of a similar nature, regardless of the industry represented by the program, or any combination thereof. Excluded from this definition are real estate investment trusts, tax qualified pension and profit sharing plans pursuant to Sections 401 and 403(a) of the Internal Revenue Code and individual retirement plans under Section 408 of that Code, tax sheltered annuities pursuant to the provisions of Section 403(b) of the Internal Revenue Code and any company including separate accounts registered pursuant to the Investment Company Act of 1940.
- (f) Limited Principal - Options
- (1) All persons associated with a member who are included within the scope of Part II, Section 1 hereof, shall register with the Corporation as a Limited Principal - Options if:
- a. their activities in the investment banking and securities business will include the solicitation, sale, endorsement and/or writing of securities options;
  - b. prior to or concurrent with such registration they become registered and qualified as a General Securities Representative; and,
  - c. they pass the appropriate Qualification Examination for Limited Principal - Options or an equivalent examination acceptable to the Corporation.

(2) Grandfather Clause - Any person who has been registered with a member as a principal for a period of three years prior to \_\_\_\_\_, and his activities in the investment banking or securities business involved the solicitation, sale, endorsement and/or writing of securities options for the member for that period shall not be required to take the Qualification Examination for Limited Principal - Options to qualify and register as a Limited Principal - Options, subject to the provisions of Part II, Section I(d) hereof.

(3) Persons registered solely as a Limited Principal - Options shall not be qualified to function in a principal capacity with responsibility over any area of business activity not prescribed in this subsection (f).

(g) Limited Principal - Securities Trading

(1) All persons associated with a member who are included within the scope of Part II, Section 1 hereof, shall, unless they are registered as General Securities Principals, take and pass the appropriate Qualification Examination for Limited Principal - Securities Trading and register with the Corporation as such if:

- a. their activities in the investment banking and securities business are limited solely to exercising discretionary authority in trading securities and/or effecting market making securities transactions in the over-the-counter securities markets for or on behalf of the member; and,
- b. prior to or concurrent with such registration they become registered and qualified as either a General Securities Representative or as a Securities Trader Representative.

(2) Persons registered solely as a Limited Principal - Securities Trading shall not be qualified to function in a principal capacity with responsibility over any area of business activity not prescribed in this subsection (g).

(3) Persons registered as a Limited Principal - Securities Trading shall not be qualified to solicit, sell and/or otherwise personally service accounts of public customers unless also qualified and registered in another principal or representative category, the provisions of which specifically provide for such activity.

Section 3 - Registration of Representatives

(a) Registration Requirements - All persons associated with a member who are to function as registered representatives shall be registered as

such with the Corporation in the category of registration appropriate to the function to be performed as specified in Section 4 hereof. Before their registration can become effective, they shall pass a Qualification Examination for Registered Representatives appropriate to the category of registration.

(b) Definition of Representative - The term "representative" shall mean a person associated with a member not otherwise required to register as a principal, including assistant officers other than principals, who is engaged in the investment banking or securities business for the member. Such shall include but not necessarily be limited to those persons:

- (1) whose duties include the solicitation, sale or trading of securities;
- (2) with supervisory responsibility over the activities of registered representatives;
- (3) designated by the member as having supervisory responsibility for the member's compliance with the rules and regulations of the Corporation, the Securities and Exchange Commission and all applicable federal securities laws; or,
- (4) engaged in and responsible for the training of persons associated with a member for any of those functions.

(c) Registration of Persons Engaged in Training - All persons associated with a member engaged in the training of persons whose activities in the investment banking or securities business encompass functions which require registration in one or more of the categories described in Sections 4(a) through 4(e) hereof, shall be required to qualify and register in a category of representative registration at least equivalent to that for which they are training such persons unless they are otherwise required to be registered as principals.

(d) Requirement for Examination on Lapse of Registration - Any registered representative whose most recent registration as such has been terminated for a period of two or more years immediately preceding the date of receipt by the Association of a new application shall be required to pass a Qualification Examination for Representatives appropriate to the category of registration as specified in Section 4 hereof unless such person has been continuously registered with the Corporation as a principal.

(e) Waiver of Requirement to Take Qualification Examination - In exceptional cases and where good cause is shown, the President of the Corporation, or his delegate, upon request by the member, may waive the require-

ment to take a Qualification Examination. All such requests shall be in writing, addressed to the President of the Corporation and signed by a registered principal of the requesting firm. Advanced age, physical infirmity or experience in fields ancillary to the investment banking or securities business will not individually of themselves constitute sufficient grounds to waive the requirement to take a Qualification Examination. A request for a waiver based solely upon the expiration of the two year period since the most recent registration with the Association will not be honored. Extensions of time beyond that specified within this Schedule will not be granted. Except where otherwise specified herein, Qualification Examinations required hereby shall be taken and passed by the applicant and the member shall receive notification of such from the NASD prior to the performance by the applicant of the functions for which he is seeking registration.

(f) Grandfather Clause - Any person who was registered with the Corporation as a representative on or before September 1, 1974, shall not be required to pass a Qualification Examination for any category of registration specified in Part II, Section 4 hereof, and shall automatically be registered as a General Securities Representative subject to the provisions of subsection (d) hereof. Any person registered with the Corporation after September 1, 1974, shall be registered with the Corporation in the appropriate category of representative registration for which a Qualification Examination had been taken and passed, subject to the provisions of subsection (d) hereof.

#### Section 4 - Categories of Registration of Representatives

(a) General Securities Representative - All persons associated with a member whose activities in the investment banking or securities business include the solicitation or sale of securities generally; the supervision of General Securities Representatives; and, responsibility for the member's compliance with the rules and regulations of the Corporation, the Securities and Exchange Commission and all applicable federal securities laws shall be required to register with the Corporation as a General Securities Representative unless otherwise required to be registered as a principal. Persons whose activities in the investment banking or securities business encompass only functions which would only require their registration in one or more of categories (b) through (e) hereof, may, at their discretion, be registered as General Securities Representatives.

(b) Securities Trader Representative - All persons associated with a member whose activities in the investment banking or securities business are limited solely to exercising discretionary authority in trading securities and/or effecting market making securities transactions in the over-the-counter



securities markets for the member shall be required to register with the Corporation as a Securities Trader Representative if not otherwise required to register as a principal. A person registered solely as a Securities Trader Representative may not solicit, sell and/or otherwise personally service accounts of public customers.

(c) Investment Company and Variable Contracts Products Representative - All persons associated with a member whose activities in the investment banking or securities business are limited solely to the solicitation and/or sale of securities of companies registered pursuant to the Investment Company Act of 1940, variable contracts products and insurance premium funding programs registered pursuant to the Securities Act of 1933 shall, unless qualified and registered as a General Securities Representative, be required to register with the Corporation as an Investment Company and Variable Contracts Products Representative.

(d) Direct Participation Programs Representative - All persons associated with a member whose activities in the investment banking or securities business are limited solely to the solicitation and/or sale of direct participation programs shall, unless qualified and registered as a General Securities Representative, be required to register with the Corporation as a Direct Participation Programs Representative.

(e) Real Estate Securities Representative - All persons associated with a member whose activities in the investment banking and securities business will be limited solely to the solicitation and sale of any certificate of interest or participation, partnership interest, investment contract or other interest or instrument constituting a security as defined in Section 2(1) of the Securities Act of 1933 which represents principally the acquisition, investment or holding of real property or an interest therein (except corporate securities, real estate investment trusts or any other securities of a legal entity which is designed to provide a public trading market for the securities) shall, unless qualified and registered as either a General Securities Representative or as a Direct Participation Programs Representative, be required to register with the Corporation as a Real Estate Securities Representative.

## Section 5 - Special Situations

### (a) Current Registration With SECO

- (1) Persons associated with a member who are currently qualified to engage directly or indirectly in securities activities with a non-member broker/dealer as a result of having taken and passed an examination pursuant to the provisions of Section 15(b)(8) of the Securities Exchange Act of 1934, as amended, and Rule 15b8-1

thereunder, more commonly known and hereafter referred to as the SECO examination, or were not required to take the SECO examination because of the exemption provided in Rule 15b8-1, for persons who were broker/dealers or became associated persons prior to July 1, 1963, and have been continuously registered as such since that date shall not be required, in order to become registered as a representative of a member of the Corporation, to take and pass a Qualification Examination for Registered Representatives appropriate to the category of registration applied for unless he has been terminated with the non-member broker/dealer for two or more years. All such persons shall, however, be required to take and pass an examination based on the Corporation's rules and regulations before they may function as registered representatives with a member in any category of registration.

- (2) Persons associated with a member who have not taken the SECO examination but who have become and are currently qualified pursuant to the provisions of Section 15(b)(8) of the Securities Exchange Act of 1934, as amended, and Rule 15b8-1 thereunder, as a result of acceptance by the Securities and Exchange Commission of a securities examination administered by and for a state securities administration and successfully completed by the applicant, shall be required, unless that state's examination is also accepted by the Corporation, to take the appropriate Qualification Examination for Registered Representatives unless he has been fully registered pursuant to the referred to Section 15(b)(8) and Rule 15b8-1 for at least one year immediately preceding the receipt of his application by the Corporation. All such persons who are not required to take any Qualification Examination for Registered Representatives because of the one year experience factor shall, however, be required to successfully complete an examination based upon the Corporation's rules and regulations before he may function as a registered representative with a member.

(b) Foreign Associates

- (1) Exemption From Registration and Qualification Examination - All persons associated with a member who are to function as foreign associates shall not be required to register with the Corporation and shall be exempt from the requirement to pass a Qualification Examination.
- (2) Definition of Foreign Associate - The term "foreign associate" shall mean a person associated with a member:

- a. who is not a citizen, national or resident of the United States or any of its territories or possessions; and,
  - b. who will conduct all his securities activities in areas outside the jurisdiction of the United States and will not engage in any securities activities with or for any citizen, national or resident of the United States.
- (3) Requirement of Application for Foreign Associate - Prior to the time the exemption provided for in subsection (b)(1) hereof may become effective, the member desiring to employ any such person must file with the Corporation a form designated Application for Classification as a Foreign Associate for each such person and must certify that such person meets the two criteria contained in subsection (b)(1) hereof as well as that:
- a. such person is not subject to any of the prohibitions to registration with the Corporation contained in Article I, Section 2(a) through 2(d) of the By-Laws of the Corporation; and,
  - b. service of process for any proceeding instituted by the Corporation in respect to such person may be sent to an address in the United States at an office of the member. The member will be responsible for responding to the Association if the individual cannot be served.
- (4) Termination of Employment - In the event of termination of the employment of a foreign associate, the member must notify the Corporation immediately by filing a notice of termination as required by Article XV, Section 5, of the By-Laws.

#### Section 6 - Persons Exempt From Registration

- (a) The following persons associated with a member are not required to be registered with the Corporation:
- (1) Persons associated with a member whose functions are solely and exclusively clerical or ministerial;
  - (2) Persons associated with a member who are not actively engaged in the investment banking or securities business;
  - (3) Persons associated with a member whose functions are related solely and exclusively to the member's need for nominal corporate officers or for capital participation; and,

- (4) Persons associated with a member whose functions are related solely and exclusively to:
- a. transactions on a registered national securities exchange and who are registered with such exchange;
  - b. transactions in exempted securities; or,
  - c. transactions in commodities.

(b) In every instance where exemption is requested or applicable, except pursuant to the provisions of subsections (a)(1) and (2) hereof, the member must file on a form\* designated by the Board of Governors with the Corporation within ten (10) business days of either the date the person becomes associated with the member or the date on which the exemptive provisions become applicable to him.

#### Section 7 - Qualification Examinations and Procedures

(a) Study Outlines - Qualification Examinations for the various categories of principals and representatives specified in this Schedule C shall consist of a series of questions based upon topics outlined in study outlines provided by the Corporation, a list of which is available from the Department of Qualifications and Examinations.

(b) Time and Place - Examinations shall be given at such times and places and under such conditions as shall be prescribed by the Board of Governors.

(c) Grading Scale - Examination results shall be reported to the member firms on a pass/fail basis only. Failing grades will be accompanied by an analysis of the candidate's performance on the examination. Passing scores assigned to each examination series shall be determined by the Board of Governors, or its designated agent.

(d) Procedure Upon Failing Examination - Applicants who fail an examination may, subject to the payment of required examination fees and receipt of a new admission certificate, retake such examination up to three times without waiting any specified period of time between attempts. If an examination is failed three times, the applicant must wait 90 days before again taking the examination and between each subsequent attempt. A new admission certificate will not be issued in connection with any examination until proper fees for the examination have been received by the Corporation. Proctors will admit only those candidates having a valid admission certificate.

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\*The form currently designated for this purpose is Form EX-1.

(e) Assistance During Examination - An applicant cannot receive assistance while taking the examination. Each applicant shall certify to the Board of Governors that no assistance was given to or received by him during the examination.

(f) Confidentiality of Examinations - The Corporation considers all of its Qualification Examinations to be highly confidential. The removal from an examination center, reproduction, disclosure, receipt from or passing to any person, or use for study purposes of any portion of any Qualification Examination, whether of present or past series, or any other use which would compromise the effectiveness of the Qualification Examinations and the use in any manner and at any time of the questions or answers to the Qualification Examinations are prohibited and are deemed to be a violation of Article III, Section 1, of the Rules of Fair Practice.

(g) SECO Grace Period - The President of the Corporation, or his delegate, in the case of a broker/dealer applicant for membership in the Corporation who was previously qualified, and at the time of his application for membership is currently qualified, pursuant to the provisions of Section 15(b)(8) of the Securities Exchange Act of 1934, as amended, and Rule 15b8-1 thereunder, shall have the discretion to grant a grace period of reasonable and stated duration after the effective date of membership of the applicant during which period of time the persons associated with the member who were previously, and at the time of their applications are, qualified pursuant to the aforementioned Section 15(b)(8) and Rule 15b8-1 may actively engage in the investment banking or securities business while qualifying as registered representatives and principals; provided, however, the provisions of this subsection shall in no way be construed so as to contravene the minimum qualifications for membership in respect to principals required pursuant to the provisions of Part I of this Schedule C. In no event may the said grace period exceed one year from the effective date of membership of the applicant. If the referred to persons associated with the member do not qualify, pursuant to Schedule C, by the date of the expiration of the grace period, they shall no longer be permitted to engage in the investment banking or securities business until they qualify thereunder. In no case shall a person not currently qualified under Section 15(b)(8) and Rule 15b8-1 be permitted to act as a representative or principal of the member during the grace period unless he has qualified pursuant to the provisions of Schedule C.

**NASD**

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.  
1735 K STREET NORTHWEST • WASHINGTON D.C. 20006

March 31, 1975

TO: All NASD Members and Interested Persons

RE: Proposed Amendment to Appendix C of Article III, Section 32  
Rules of Fair Practice

The Board of Governors of the Association has proposed amendments to the Mandatory Fidelity Bonding Rule which is being published by the Board at this time to enable all interested persons an opportunity to comment thereon. Such comments must be in writing and must be received by April 30, 1975 in order to receive consideration.

Article III, Section 32 authorized the Board to amend or modify the provisions of Appendix C without recourse to the membership for vote. After the comment period has expired the proposed amendments must again be reviewed by the Board. If the changes, or an amended version thereof, are at that time approved by the Board they must then be submitted to and not disapproved by the Securities and Exchange Commission prior to becoming effective.

Any comments should be addressed to Mr. Donald H. Burns, Secretary, National Association of Securities Dealers, Inc., 1735 K Street, N.W., Washington, D.C. 20006, on or before April 30, 1975. All communications will be considered available for inspection.

Sincerely,



Frank J. Wilson  
Senior Vice President  
Regulation

Explanation of Proposed Amendment

The proposed amendment, which involves the addition of a new subsection (b) (2) to Appendix C, permits the inclusion of a deductible provision in a fidelity bond when a member purchases coverage in an amount greater than that required under the rule. For example - A member who is required to obtain a fidelity bond in the amount of \$30,000 is currently permitted a maximum deductible of up to \$5,000 or 10% of the required amount of the bond, whichever is greater. In this instance, the member could include a maximum \$5,000 deductible amount. If the member purchased a \$100,000 bond instead, the maximum deductible under existing Appendix C would remain at \$5,000.

In the same situation, under the proposed amendment to Appendix C, the maximum deductible would be \$10,000 since the permitted deductible will now be dependent upon the amount of the bond obtained rather than the amount of the bond required.

With an increased maximum deductible, a member who wishes to purchase more than the minimum coverage required could pay a smaller premium than is possible under the current rule for the same amount of coverage.

An increased deductible, however, exposes a members' capital to a greater risk of loss from claims falling within the deductible limit. The Board believes, therefore, that this increased risk should be self-insured by a member who takes advantage of the increased deductible provision. Consequently, the amendment provides that such members would be required to deduct the excess amount of the deductible from their net worth when calculating their minimum required net capital under SEC Rule 15c3-1 (the net capital rule).

Text of Proposed Amendment  
(added language underlined)

It is proposed that Appendix C to Section 32 of the Rules of Fair Practice be amended by adding a new subsection (b) (2) thereto as indicated by the underlined language below:

Deductible Provision:

- (b) (1) A deductible provision may be included in the bond of up to \$5,000 or 10% of the minimum insurance requirement established hereby, whichever is greater.
- (2) If a member desires to maintain coverage in excess of the minimum insurance requirement

then a deductible provision may be included in the bond of up to \$5,000 or 10% of the amount of blanket coverage provided in the bond purchased, whichever is greater. The excess of any such deductible amount over the maximum permissible deductible amount described in paragraph (b) (1) above must be deducted from the member's net worth in the calculation of the member's net capital for purposes of rule 15c3-1 under the Securities Exchange Act of 1934.