

proposals they filed with the Commission.¹⁹

Other concerns were raised with respect to the Regulatory Element, including its cost and focus (some found its scope too broad, others too narrow). Concern also was expressed that the re-entry provision's disciplinary fine threshold was ambiguous as written and could be unfair in application. Other commenters focused on the statistics to be generated by the Regulatory Element. Specifically, they were concerned about the types of statistics that would be available, and the intended and acceptable uses of such statistics.

Several commenters were concerned that the Regulatory Element would only be administered at NASD operated testing centers. Suggested alternatives included administering the Regulatory Element at firms, subject to appropriate controls, and reliance on third party interactive programs similar to those provided to the futures industry.

One commenter suggested that the securities industry model the Regulatory Element after state insurance continuing education programs, in which the licensing authority imposes the regulatory requirement directly on the individual, rather than on the firm. Another suggestion was that the Central Registration Depository ("CRD")²⁰ help firms comply with the Regulatory Element. Specifically, CRD could be used by firms to determine the length of service of their registered persons and to identify those that would be subject to the Regulatory Element in each of the next few years.

B. Comments Regarding the Firm Element

A concern expressed by several commenters regarding the Firm Element was the cost it will impose on smaller firms. To mitigate this effect, it was suggested that the SROs prepare and administer training programs; provide subsidies to smaller firms to help them comply with the Firm Element; or that a video satellite program be created that would enable firms to secure qualified speakers, and include material that would comply with the Firm Element.

Several commenters stated that the standards for the Firm Element are too vague to allow firms to ensure proper compliance. Some commenters suggested that the Firm Element focus on suitability, and that some form of

pre-approval be provided regarding the contents of a firm's program. Another commenter questioned the usefulness of feedback from the Regulatory Element in developing an appropriate Firm Element. Concern also was expressed regarding the apparent authority of an SRO arbitrarily to prescribe specific training for a member firm. Finally, there was uncertainty regarding those who would be deemed "covered persons."

C. Response to Comments

In their filings with the Commission, the SROs addressed certain of the commenters' concerns by making three technical changes to the Regulatory Element portion of the rules as originally drafted. First, the SROs revised the rules to state clearly that registered persons must participate in the Regulatory Element on three occasions: after the occurrence of their second, fifth, and tenth registration anniversary dates. Second, the SROs expanded the provision concerning failure to complete the Regulatory Element to state that a registration that is inactive for a period of two calendar years would be terminated administratively, and that a person whose registration is so terminated must requalify by taking the appropriate examination, before such person's registration could be reactivated. Third, the SROs revised the re-entry provision of the Regulatory Element to clarify that a securities governmental agency or securities SRO could only require re-entry into the program in connection with a sanction in a disciplinary action. This change is meant to address the concerns of those commenting on the due process issues that could arise if regulatory authorities were able to mandate re-entry arbitrarily.

In response to comments received, the Council has stated that the CRD system will be used to track and communicate anniversary dates and evidence of completion of the Regulatory Element. The Regulatory Element's computer based systems will also capture, store, and analyze data that will indicate who took the training, when, and where, as well as other information.

V. Discussion

The Commission believes that the SROs' proposed rule changes are consistent with the requirements of the Act and the rules and regulations thereunder applicable to national securities exchanges, national securities associations, and the MSRB and, in particular, the respective requirements of Sections 6(b)(5), 15A(b)(6), and

15B(b)(2)(C) of the Act.²¹ Sections 6(b)(5), 15A(b)(6), and 15B(b)(2)(C) require, among other things, that the rules of an exchange, an association, or the MSRB, respectively, be designed to promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, protect investors and the public interest. The Commission further believes that the proposed rule changes also are consistent with the respective provisions of Sections 6(c)(3)(B), 15A(g)(3)(A), and 15B(b)(2)(A) of the Act,²² each of which makes it the responsibility of an exchange, an association, or the MSRB to prescribe standards of training, experience and competence for persons associated with SRO members.

The Commission also believes that the proposed rule change is consistent with the purposes underlying Section 15(b)(7) of the Act,²³ which generally prohibits a registered broker-dealer from effecting any transaction in, or inducing the purchase or sale of, any security unless such broker-dealer meets the standards of training, experience, competence, and other qualifications as the Commission finds necessary or appropriate in the public interest or for the protection of investors.²⁴ The Commission believes that the SROs' proposals to impose affirmative obligations on registered persons on a continuing basis are an appropriate means of maintaining and reinforcing the qualification standards applicable when a person first is registered. Moreover, it is Commission policy to rely principally on the SROs for the formulation and administration of qualification standards, subject to Commission review and oversight.²⁵

The SROs' proposals convey broadly applicable information relating to compliance, regulatory, ethical, and general sales practice standards, as well as job related material for specific professional areas and products. The SROs have divided the continuing

²¹ 15 U.S.C. §§ 78f(b)(5), 78o-3(b)(6), and 78o-4(b)(2)(C) (1988).

²² 15 U.S.C. §§ 78f(c)(3)(B), 78o-3(g)(3)(A), and 78o-4(b)(2)(A) (1988).

²³ 15 U.S.C. § 78o(b)(7) (1988).

²⁴ *Id.*

²⁵ See Rule 15b7-1 under the Act, 17 CFR 240.15b7-1 (1994), and Securities Exchange Act Release No. 32261 (May 4, 1993), 58 FR 27656 (May 11, 1993) (in adopting Rule 15b7-1 to require broker-dealers to comply with SRO qualification standards, the Commission stated that it has been longstanding Commission policy to rely principally on the SROs in the formulation and administration of qualification standards, subject to Commission review and oversight).

¹⁹ See *infra*, Part IV, Section C.

²⁰ CRD is a computerized filing and data processing system operated by the NASD that maintains registration information regarding registered broker-dealers and their registered personnel for access by state regulators, SROs, and the Commission.