

APPENDIX A
TO
REPORT AND RECOMMENDATIONS OF THE TASK FORCE
ON PRIVATE PLACEMENT BROKER-DEALERS

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This Appendix A contains information relating to present requirements for forming a broker-dealer through the NASD process provided in Rules 1013 and 1014 of the Membership and Registration Rules.

In addition to compliance with the NASD requirements, firms must be concerned about both understanding and complying with the SEC requirements for broker-dealers found in both the Securities Exchange Act of 1934 and the rules promulgated thereunder, together with the myriad of cases, interpretations, speeches, and informal positions that constitute the body of law with which broker-dealer must comply. While the NASD does the review of new firm applications, and the SEC does not review them, the NASD review contemplates establishing the firm's understanding of and compliance with certain federal securities law requirements. The SEC also provides a helpful *Division of Market Regulation: Compliance Guide to the Registration and Regulation of Broker-Dealers* which can be found on its website.

Beyond the SEC requirements, new firms must register with each state in which they plan to do business. States also require registration of agents of the broker-dealer and certain management personnel. There is no collective state review so an applicant will be reviewed independently in each state. Times for that review and that process that is followed varies dramatically among the states.

The process of forming a broker-dealer can take up to six months and occasionally longer. The quality of preparation of the application, as well as backlogs at the District office can dramatically affect turnaround. The NASD is attempting to expedite the process this year, but there is substantial waiting time before a registration application can be filed, since the task of preparing the 1014 filing is highly time-consuming if done correctly from the start of the process. Applications move at a far more expedited process if properly prepared in the first instance.

Rule 1013 requires filing of an application with a variety of prescribed documents, a pre-membership interview in the District office, and a membership agreement imposed by the NASDR under which the firm must operate unless and until modified by the NASDR. Much of the information required to fulfill this requirement is not addressed in a form, but rather the firm must create documents establishing compliance.

The new member application is filed with the District office and includes:

- Paper Form BD for the firm and Forms U-4 for individuals.
- Disclosures regarding disciplinary history.

- If applicable, heightened supervision procedures for representatives having a disciplinary history and in some other situations.
- Contracts with banks, services bureaus, clearing firms, and other vendors.
- Description of capital sources and related documentation.
- Written supervisory procedures manual and compliance manual.
- Training program.
- Record-keeping systems.
- Privacy and information sharing policies.
- Anti-money laundering policies and procedures.

The NASD's *How To* instructions for preparing the application are quite detailed.

In addition to the requirements for the firm itself, individuals associated with the firm must pass not only examinations required for registered representatives, but also as principals including a General Securities, Financial and Operational, and special categories such as options and municipal securities. These are detailed in the summary provided in Attachment 4 to this Appendix. The states require completion of the Series 63 examination. Many states require only general securities examination and a state examination completion and defer to the NASD on regulation of principals. Study materials for examination are available, but most people entering the business will attend training classes.

The firm must develop the capacity for filings its forms on the Central Registration Depository.

Naturally the NASD and the states charge fees for registration. The SEC does not have a fee. It makes the registration of the firm effective upon notice from the NASD.

Finally a firm may required to be a member of the Securities Investors Protection Corporation and pay assessments for that purpose. Bonding is also required by the NASD and the states.

We have provided the following documents relevant to our discussion of the review process:

Attachment 1 Requirements imposed by NASD Rule 1013.

Attachment 2 Requirements imposed by NASD Rule 1014.

Attachment 3 SEC Form BD.

Attachment 4 Summary of NASD Examination Requirements.

Attachment 5 Proposed reduction of review procedures for PPBD.

Attachment 6 Proposed revisions to Form BD for PPBD - Titled Form BD-EZ.

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