

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-49314; File Nos. SR-NYSE-2004-03; SR-NASD-2004-020)

February 24, 2004

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Changes by the New York Stock Exchange, Inc. and the National Association of Securities Dealers, Inc. Relating to Certain Prerequisites to and Exemptions from Taking the Research Analyst Qualification Examination (“Series 86/87”)

Pursuant to Section 19(b)(1)¹ of the Securities Exchange Act of 1934 (the “Act” or “Exchange Act”), and Rule 19b-4 thereunder,² notice is hereby given that on January 30, 2004, the New York Stock Exchange, Inc. (“NYSE” or the “Exchange”), and on February 3, 2004, the National Association of Securities Dealers, Inc. (“NASD”), filed with the Securities and Exchange Commission (“SEC” or the “Commission”) the proposed rule changes as described in Items I, II, and III below, which Items have been prepared by the respective self-regulatory organizations (“SROs”). The Commission is publishing this notice to solicit comments on the proposed rule changes from interested persons.

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

The NYSE is proposing an interpretation to NYSE Rule 344 to establish certain prerequisites to, and exemptions from, taking the Research Analyst Qualification Examination (“Series 86/87”).

NASD is proposing to amend NASD Rule 1050 to set forth certain prerequisites and exemptions for the requirement that all associated persons who function as research

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

analysts be registered with NASD and pass a qualification examination. Specifically, the proposed rule change would (1) establish, as a prerequisite to be registered as a research analyst, the requirement that an applicant also be registered pursuant to NASD Rule 1032 as a General Securities Representative and (2) provide for an exemption from the analytical portion of the Research Analyst Qualification Examination (Series 86) for certain applicants who have passed both Levels I and II of the Chartered Financial Analyst (“CFA”) Examination.

Below is the text of the proposed rule changes. Proposed new language is in *italics*; proposed deletions are in [brackets].

A. NYSE’s Proposed Interpretation Text

NYSE Rule 344 RESEARCH ANALYSTS AND SUPERVISORY ANALYSTS

/01 Qualifications

Research Analyst candidates shall qualify by taking the Research Analyst Qualification Examination (Series 86/87). For purposes of this interpretation, the term “research analyst” is defined in Rule 344.10. The Series 86 covers fundamental security analysis and valuation of equity securities. The Series 87 covers pertinent rules and regulations of the self-regulatory organizations, and the SEC.

Supervisory Analyst candidates shall qualify by taking and passing the Supervisory Analyst (Series 16) Examination.

Pre-requisite

The General Securities Registered Representative Examination (Series 7) qualification is a prerequisite for any Research Analyst candidate prior to

taking either Part I (Series 86) or Part II (Series 87) of the Research Analyst Qualification Examination.

Alternatively, the United Kingdom Limited Registered Representative (Series 17) Examination and the Canadian Limited Registered Representative (Series 37/38) Examination will also serve as prerequisites to taking either Part I or Part II of the Research Analyst Qualification Examination.

In satisfying the Series 7, Series 17 or Series 37/38 examination prerequisite, Research Analyst candidates will not be required to complete the four month post-examination training period required of Registered Representative candidates pursuant to Rule 345.15/02 (see page 3459). Candidates that have failed either Part I or II of the examination must wait 30 days before retaking either part of the examination.

Experience

Appropriate experience for a candidate for Supervisory Analyst means having at least three years prior experience within the immediately preceding six years involving securities or financial analysis.

Examples of appropriate experience may include the following:

- (a) Equity or Fixed Income Research Analyst;
- (b) Credit Analyst for a securities rating agency;
- (c) Supervising preparation of materials prepared by financial/securities analysts;

- (d) Financial analytical experience gained at banks, insurance companies or other financial institutions;
- (e) Academic experience relating to the financial/securities markets/industry.

/02 Director of Research

A person having the title of “Director of Research” need not be a supervisory analyst as defined by the Rule so long as he does not approve research reports. If, however, such a person is in charge of registered representatives, he must qualify as a supervisory person under Rule 342.13.

/03 Chartered Financial Analyst (CFA)

Successful completion of the CFA Level I Examination given by the Institute of Chartered Financial Analysts (in lieu of completion of Levels, I, II and III for a full CFA designation) will suffice to allow a Supervisory Analyst candidate to qualify by taking Part I of the Series 16 Qualification Examination.

Successful completion of Levels I and II of the CFA Examination allows a Research Analyst candidate to request an exemption from Part I (Series 86) of the Research Analyst Qualification Examination. If an exemption is granted for Part I (Series 86), a candidate will be qualified as a Research Analyst after passing Part II (Series 87) only.

To qualify for a CFA exemption a Research Analyst candidate must have:
(i) completed the CFA Part II within two years of application for
registration or (ii) functioned as a research analyst continuously since
having passed the CFA Part II. Applicants that have completed the CFA
Part II that do not meet criteria (i) or (ii) where good cause is shown based
upon previous related employment experience may make a written request
to the Exchange for an exemption.

B. NASD's Proposed Rule Text

1050. Registration of Research Analysts

(a) All persons associated with a member who are to function as research
analysts shall be registered with NASD. Before [their] registration[s] as a Research
Analyst can become effective, [they]an applicant shall:

(1) be registered pursuant to Rule 1032 as a General Securities
Representative; and

(2) pass a Qualification Examination for Research Analysts as specified
by the Board of Governors.

(b) For the purposes of this Rule 1050, "research analyst" shall mean an
associated person who is primarily responsible for the preparation of the substance of a
research report or whose name appears on a research report.

(c) Upon written request pursuant to the Rule 9600 Series, NASD will grant a
waiver from the analytical portion of the Research Analyst Qualification Examination
(Series 86) upon verification that the applicant has passed Levels I and II of the Charter
Financial Analyst Examination and has either (1) functioned as a research analyst

continuously since having passed the Level II examination or (2) applied for registration as a research analyst within two years of having passed the Level II examination. An applicant who has been granted such an exemption still must become registered as a General Securities Representative and then complete the regulatory portion of the Research Analyst Qualification Examination (Series 87) before that applicant can be registered as a Research Analyst.

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9600. PROCEDURES FOR EXEMPTIONS

9610. Application

(a) Where to File

A member seeking exemptive relief as permitted under Rules 1021, 1050, 1070, 2210, 2315, 2320, 2340, 2520, 2710, 2720, 2810, 2850, 2851, 2860, Interpretive Material 2860-1, 3010(b)(2), 3020, 3150, 3210, 3230, 3350, 8211, 8212, 8213, 11870, or 11900, Interpretive Material 2110-1, or Municipal Securities Rulemaking Board Rule G-37 shall file a written application with the appropriate department or staff of the Association and provide a copy of the application to the Office of General Counsel of NASD Regulation.

(b) through (c) No change.

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

In their filings with the Commission, the NYSE and NASD included statements concerning the purpose of and basis for the proposed rule changes. The text of these

statements may be examined at the places specified in Item IV below. NYSE and NASD have prepared summaries, set forth in Sections A, B, and C below.

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

1. NYSE’s Purpose

Recent amendments to NYSE Rule 344 (“Research Analysts and Supervisory Analysts”) require Research Analysts to be registered with, qualified by, and approved by the Exchange. The Exchange is proposing to adopt a new interpretation to NYSE Rule 344 to establish certain prerequisites to and exemptions from the requirement that Research Analysts pass a new qualification examination.

Background

On July 29, 2003, the SEC approved amendments to Exchange Rules 472 (“Communications with the Public”), 351 (“Reporting Requirements”), 344 (“Research Analysts and Supervisory Analysts” (formerly titled “Supervisory Analysts”)), and 345A (“Continuing Education for Registered Persons”) (collectively referred to as the “Research Analysts’ Conflicts Rules”).³

The Research Analysts’ Conflicts Rules include, a new registration category and qualification examination for research analysts, address potential conflicts of interest, and require disclosure in research reports and during public appearances by research analysts of other potential conflicts of interest. The NYSE believes that the Research Analyst Qualification Examination represents a continuation of the SRO regulatory effort to safeguard the investing public from potential conflicts of interest relating to research

³ See Securities Exchange Act Release No. 48252 (July 29, 2003), 68 FR 45875

analysts. NYSE believes that the new qualification examination, in conjunction with the new rules, assist in protecting the investing public by requiring research analysts to demonstrate that they are competent to perform their jobs and are knowledgeable about the new regulatory requirements affecting them.

The Research Analyst Qualification Examination (Series 86/87) is a five-and-a-half hour examination, consisting of 150 questions. The exam is divided into two parts. Part I, the Series 86, consists of 100 questions, which address security analysis and valuation of equity securities. Candidates will be allotted 240-minutes to complete Part I. Part II, the Series 87, consists of 50 questions, which primarily address pertinent SRO and SEC rules and regulations, including the recent Research Analysts' Conflict Rules. Candidates will be allotted 90 minutes to complete Part II.

The requirement to take and pass the proposed Series 86/87 examination applies to all prospective and current research analysts, as the term is defined in Exchange Rule 344.10, which provides that the term "research analyst" includes a member, allied member, or employee who is primarily responsible for the preparation of the substance of a research report and/or whose name appears on such report. Individuals who are currently functioning as Research Analysts will be required to pass the Series 86/87 examination within one year of its implementation date.

The proposed interpretation to NYSE Rule 344 would require taking the General Securities Registered Representative Examination (Series 7) as a prerequisite to taking either Part I or Part II of the Research Analyst Qualification Examination. Although certain subject areas of the Series 7 examination are not directly related to a research

analyst's job, the knowledge required to pass the Series 7 examination will provide an analyst with good general background information on the industry and address regulatory concerns in instances when an analyst might participate in sales and solicitation activities. Moreover, the Series 7 examination which tests, among other topics, "communications with the public" and "know your customer" rules, would serve an important regulatory purpose to have research analysts Series 7 qualified.

Alternatively, the United Kingdom ("UK") Limited Registered Representative (Series 17) Examination and the Canadian Limited Registered Representative (Series 37/38) Examination will also serve as prerequisites to taking either Part I or Part II of the Research Analyst Qualification Examination. Persons qualified to conduct a general public securities business in the UK and Canada respectively can also be qualified for the same in the U.S. by taking the Series 17 or Series 37/38 in lieu of the Series 7. These examinations are intended to cover subject matter unique to the U.S. securities markets otherwise not covered by the UK/Canada examinations.

The proposed interpretation also allows a research analyst candidate that has passed both Level I and Level II of the Chartered Financial Analyst ("CFA") Examination, to request an exemption from Part I (Series 86) of the Research Analyst Qualification Examination. A Research Analyst candidate that has passed Levels I and II of the CFA Examination will have evidenced proficiency in "Investment Tools" and "Asset Valuation" (2 major topic areas of the exam). Exchange staff has reviewed the CFA Level I and II examinations and has determined that the content coverage is comparable to the Series 86. Many research analysts have completed CFA Levels I and II, and it is not necessary to re-qualify them with respect to such analytical skills. As

such, granting an exemption from the securities analysis and equity valuation part (Series 86) of the examination can be done without compromising any regulatory concerns. Analysts granted waivers of the Series 86 will still be required to pass the Series 87 dealing with industry rules and regulations.

To qualify for the CFA exemption to the examination requirement a Research Analyst candidate must have: (i) completed the CFA Part II within 2 years of application for registration or (ii) functioned as a research analyst continuously since having passed the CFA Part II. Applicants that have completed the CFA Part II that do not meet either of the above criteria, may, upon a showing of good cause based upon previous related employment experience, make a written request to the Exchange for an exemption.

2. NYSE's Statutory Basis

The statutory basis for this proposed rule change is Section 6(c)(3)(B) of the Exchange Act.⁴ Under that Section, it is the Exchange's responsibility to prescribe standards of training, experience and competence for persons associated with Exchange members and member organizations.

In addition, under Section 6(c)(3)(B) of the Exchange Act⁵, the Exchange may bar a natural person from becoming a member or person associated with a member, if such natural person does not meet such standards of training, experience and competence as prescribed by the rules of the Exchange. Pursuant to this statutory obligation, the Exchange has: (i) developed an examination that will be administered to establish that Research Analysts have attained specified levels of competence and knowledge, and (ii)

⁴ 15 U.S.C. 78f(c)(3)(B).

proposed an interpretation to establish certain requirements and pre-requisites for analysts before taking such an examination.

3. NASD's Purpose

The proposed rule change would implement certain aspects of NASD Rule 1050, which requires that associated persons who function as research analysts register with NASD and pass a qualification examination. NASD Rule 1050 is intended to ensure that research analysts possess a certain competency level to perform their jobs effectively and in accordance with applicable rules and regulations. The proposed rule change would require such persons not only to pass the Research Analyst Qualification Examination (Series 86/87), but also to be registered pursuant to NASD Rule 1032 as a General Securities Representative (Series 7, 17, 37 or 38). The proposed rule change further would provide for an exemption from the Series 86 analytical portion of the qualification examination for certain associated persons who have passed both Levels I and II of the CFA Examination administered by the Association for Investment Management and Research ("AIMR").

As to the General Representative qualification requirement, NASD believes it is important for those functioning as research analysts to be familiar with general industry rules and practices, particularly those of registered representatives, who are a primary source for distributing research. The requirement further would develop in research analysts a sensitivity to the interests of public customers who are the end users of their work product. According to NASD, the proposed Series 86/87 examination program was developed jointly by NASD and NYSE staff in consultation with a committee of research

⁵ Id.

analysts, and the committee unanimously recommended that research analysts be required to pass the Series 7 in addition to a more job-specific research analyst qualification examination.⁶

NASD intends to require applicants to pass the Series 7 examination prior to taking the Series 86 or 87 examinations. NASD believes this is the most logical testing sequence and will provide a better foundation for applicants to understand and address the more specific topics and rules covered by the Series 86 and 87 examinations.

NASD has reviewed the content of the CFA examination and found the major areas tested in Levels I and II of that examination to be comparable to topics covered by the Series 86 examination. Moreover, NASD believes that the minimum passing scores for Levels I and II of the CFA examination are sufficient to ensure that those who succeed in passing those Levels have obtained a level of analytic competency commensurate with a passing score on the Series 86 examination. Accordingly, the proposed rule change would provide for an exemption⁷ from the Series 86 examination where an applicant has passed Levels I and II of the CFA examination and either (i) functioned as a research analyst continuously since having passed Level II or (ii) applied for registration as a research analyst within two years of having passed Level II. NASD believes these limitations will ensure that applicants have current knowledge of the concepts covered by the CFA Level I and II examinations, as well as familiarity with the

⁶ The Series 17, 37, and 38 are modified versions of the Series 7 for associated persons who are registered in good standing with the Financial Services Authority of the United Kingdom or one of the Canadian securities regulatory organizations.

current regulatory environment. Applicants who do not meet these criteria may, based upon previous related employment/experience, make written request to NASD for a waiver.⁸

An applicant who has been granted such an exemption still must become registered as a General Securities Representative and then complete the regulatory portion of the Research Analyst Qualification Examination (Series 87) before the applicant can be registered and function as a Research Analyst.

4. NASD's Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act⁹, which requires, among other things, that NASD rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that that the proposed rule change is consistent with the

⁷ Initially, the Series 86 exemption must be requested and granted manually; however, NASD anticipates that at some point the exemption will be granted automatically through the CRD system.

⁸ Pursuant to NASD Rule 1070 and the NASD Rule 9600 Series, NASD may, in exceptional cases and where good cause is shown, waive the applicable qualification examination and accept other standards as evidence of an applicant's qualifications for registration. While NASD will consider waivers of the Series 86/87 in extraordinary circumstances, in light of the purpose of the new research analyst qualification requirements, NASD does not intend to grant waivers except to those who have either passed the Series 86/87 or the CFA Levels I and II. To request either the CFA exemption or a waiver, a member must submit a written request to NASD's Testing and Qualification Department on behalf of the applicant that sets forth the basis for the request. If granted, NASD will then enter the exemption or waiver in the CRD system, which will register the applicant as a research analyst when the other examination requirements have been satisfied.

⁹ 15 U.S.C. 78o-3(b)(6).

provisions of the Act noted above in that it will ensure that those functioning as research analysts possess a minimum competency level and knowledge of applicable laws, rules and regulations, thereby enhancing investor protection.

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

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

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

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

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, or (ii) as to which the Exchange consents, the Commission:

- (a) by order approve such proposed rule change, or
- (b) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule changes are consistent with the Act. Persons making written submissions should file six copies thereof with the

Secretary, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0609. Comments may also be submitted electronically at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File Nos. SR-NYSE-2004-03, SR-NASD-2004-020. These file numbers should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, comments should be sent in hard copy or by e-mail but not by both methods.

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule changes that are filed with the Commission, and all written communications relating to the proposed rule changes between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filings will also be available for inspection and copying at the principal offices of the NYSE and NASD. All submissions should refer to the file numbers SR-NYSE-2004-03, SR-NASD-2004-020 and should be submitted by [insert date 15 days from the date of publication].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁰

Margaret H. McFarland
Deputy Secretary

¹⁰ 17 CFR 200.30-3(a)(12).