

# Financial Services

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## Effective Date of New NASD IPO Rule

### Introduction

NASD issued Notice to Members 03-79, “Initial Public Offerings (IPOs)” (the “Notice”) on December 23, 2003, announcing that new Rule 2790, “Restrictions on the Purchase and Sale of Initial Equity Public Offerings” (the “IPO Rule”), became effective that day.

The Securities and Exchange Commission approved the new IPO Rule on October 24, 2003.<sup>1</sup> The IPO Rule imposes restrictions on the distribution of initial public offerings (“IPOs”) of equity securities to securities industry insiders. The IPO Rule replaces the Free-Riding and Withholding Interpretation (IM-2110-1) (the “Interpretation”). The IPO Rule, like the Interpretation, is designed to protect the integrity of the public offering process by prohibiting securities and financial services industry insiders from taking advantage of their positions to gain access to IPOs and to promote the bona fide distribution of IPOs to the public.<sup>2</sup>

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<sup>1</sup> SEC Release No. 34-48701, *available at* <http://www.sec.gov/rules/sro/34-48701.htm>.

<sup>2</sup> For a detailed discussion of provisions of the IPO Rule, *see* Dechert Financial Services Update No. 71, “NASD Replaces ‘Hot Issues’ Interpretation with Restrictions on the Purchase and Sale of Initial Equity Public Offerings” (Nov. 12, 2003).

### Mandatory Compliance Date

The IPO Rule became effective on December 23, 2003 when it was formally announced in the Notice; however, as explained below, compliance for NASD members and associated persons is voluntary until March 23, 2004.

### Three-Month Transition Period

In response to comments raised during the rulemaking process, and in view of the number of significant changes to current practice under the Interpretation imposed by the IPO Rule, the NASD has provided for a three-month transition period (through March 22, 2004). The NASD stated in its Notice that it believes the three-month period will give members sufficient time to develop the procedures and obtain the necessary customer representations required to comply with the IPO Rule.

During the transition period, NASD members may, in connection with IPOs, comply on an account-by-account basis with either the IPO Rule or the Interpretation.<sup>3</sup> Members relying on the Interpretation may continue to rely on

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<sup>3</sup> The determination to follow either the Interpretation or the IPO Rule is made by the broker-dealer, and not by the beneficial owner of the account.

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the current interpretive and exemptive letters issued thereunder.<sup>4</sup> Members should be careful, if they choose to comply with the IPO Rule rather than the Interpretation during the transition period, to make sure that they rely on the appropriate representations to conform to the provisions of the IPO Rule, as several certifications required under the Interpretation will no longer be valid under the IPO Rule. For example, because the definition of “restricted person” under the IPO Rule is different than that under the Interpretation, hedge funds and broker-dealers should be careful during the transition period to obtain new representations from their investors/clients as to whether they are eligible to purchase new issues under the IPO Rule.

If you have questions concerning this Update or Notice to Members 03-79, please contact one of the attorneys listed below or the Dechert LLP attorney with whom you are regularly in contact:

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<sup>4</sup> It is expected that the current interpretive and exemptive letters issued under the Interpretation will be removed from the NASD website after the three-month transition period.