

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60534; File No. SR-FINRA-2009-036)

August 19, 2009

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval to a Proposed Rule Change, as Modified by Amendment No. 1, to Adopt FINRA Rules 2124 (Net Transactions with Customers), 2220 (Options Communications), 4370 (Business Continuity Plans and Emergency Contact Information) and 5250 (Payment for Market Making) in the Consolidated FINRA Rulebook

I. Introduction

On May 21, 2009, the Financial Industry Regulatory Authority, Inc (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)), filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to adopt NASD Rules 2220 (Options Communications), 2441 (Net Transactions with Customers), 2460 (Payment for Market Making), 3510 (Business Continuity Plans) and 3520 (Emergency Contact Information) as FINRA Rules in the consolidated FINRA rulebook (“Consolidated FINRA Rulebook”). The proposed rule change would renumber NASD Rule 2220 as FINRA Rule 2220, NASD Rule 2441 as FINRA Rule 2124, and NASD Rule 2460 as FINRA Rule 5250 and would combine NASD Rules 3510 and 3520 as FINRA Rule 4370 in the consolidated FINRA Rulebook. The proposed rule change was published for comment in the Federal Register on June 15, 2009.³ The Commission received one comment letter on the proposed rule change.⁴ FINRA submitted

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 60066 (June 8, 2009), 74 FR 28308 (“Notice”).

⁴ See letter from Pamela Ziermann, Dougherty and Company LLC to Elizabeth M. Murphy, Secretary, Commission, dated June 30, 2009 (“Dougherty Letter”).

a letter responding to the commenter⁵ and on July 24, 2009, filed Amendment No. 1 to the proposed rule change.⁶

II. Discussion and Commission Findings

After careful review of the proposed rule change, the comment letter, and FINRA's response, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.⁷ In particular, the Commission finds that the proposed rule change is consistent with Section 15A(b)(6) of the Act,⁸ which requires, among other things, that FINRA 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.

A. Proposed FINRA Rule 2220

FINRA is proposing to adopt NASD Rule 2220 (Options Communications) without substantive change into the Consolidated FINRA Rulebook as FINRA Rule 2220. NASD Rule 2220 sets forth a member's obligations with respect to its options communications with the public. In 2008, the Commission approved FINRA's proposed revisions to NASD Rule 2220 to make it more consistent with FINRA's general rules on communications with the public and the options communications rules of other self-regulatory organizations ("SROs").⁹ The amended

⁵ See letter from Patricia Albrecht, Assistant General Counsel, FINRA, to Elizabeth M. Murphy, Secretary, Commission, dated July 24, 2009.

⁶ In Amendment No. 1, FINRA would revise proposed FINRA Rule 4370 to require that only one of a member's two designated emergency contact persons must be a member of senior management and a registered principal of the firm.

⁷ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

⁸ 15 U.S.C. 78o-3(b)(6).

⁹ See Securities Exchange Act Release No. 58738 (October 6, 2008), 73 FR 60371 (October 10, 2008) (order approving File No. SR-FINRA-2008-013).

rule became effective on March 4, 2009.¹⁰ As amended, NASD Rule 2220, among other things: (1) uses, to the extent appropriate, the same terminology and definitions as in FINRA’s general rules on communications with the public; (2) makes the requirements for principal review of correspondence concerning options the same as for correspondence generally; and (3) updates the standards on the content of communications that precede the delivery of the options disclosure document (ODD). The Commission believes that it is appropriate to transfer NASD Rule 2220 into the Consolidated FINRA Rulebook as FINRA Rule 2220 with the non-substantive changes proposed by FINRA.

B. Proposed FINRA Rule 2124

FINRA is proposing to adopt NASD Rule 2441 (Net Transactions with Customers) without substantive change into the Consolidated FINRA Rulebook as FINRA Rule 2124. NASD Rule 2441 requires members to provide disclosure and obtain consent when trading on a “net” basis with customers.¹¹ The Commission approved NASD Rule 2441 in 2006.¹² With respect to non-institutional customers, the member must obtain the customer’s written consent on an order-by-order basis prior to executing the transaction and such consent must evidence the customer’s understanding of the terms and conditions of the order. With respect to institutional customers, a member must obtain the customer’s consent prior to executing the transaction and such consent may be obtained by either: (1) use of a negative consent letter; (2) oral disclosure and consent on an order-by-order basis; or (3) written consent on an order-by-order basis. The

¹⁰ See Regulatory Notice 08-73 (December 2008) (SEC Approves Amendments to NASD Rule 2220 to Update the Standards for Options Communications). There is no longer a comparable Incorporated NYSE Rule. FINRA previously deleted substantially similar Incorporated NYSE Rule 791 (Communications to Customers) as part of a rule change that, among other things, reduced regulatory duplication for Dual Members during the interim period before the completion of the Consolidated FINRA Rulebook. See Securities Exchange Act Release No. 58533 (September 12, 2008), 73 FR 54652 (September 22, 2008) (order approving File No. SR-FINRA-2008-036).

Commission believes that it is appropriate to transfer NASD Rule 2441 into the Consolidated FINRA Rulebook as FINRA Rule 2124 with the non-substantive changes proposed by FINRA.

C. Proposed FINRA Rule 5250

FINRA is proposing to adopt NASD Rule 2460 (Payment for Market Making) without substantive change into the Consolidated FINRA Rulebook as FINRA Rule 5250. The Commission approved NASD Rule 2460 in 1997.¹³ NASD Rule 2460 prohibits any payments by an issuer or an issuer's affiliates and promoters, directly or indirectly, to a member or person associated with a member for publishing a quotation, acting as a market maker, or submitting an application in connection therewith. The rule contains two exceptions that permit a member to accept: (1) payment for bona fide services, including, but not limited to, investment banking services; and (2) reimbursement for registration or listing fees. The Commission believes that it is appropriate to transfer NASD Rule 2460 into the Consolidated FINRA Rulebook as FINRA Rule 5250 with the non-substantive changes proposed by FINRA.

D. Proposed FINRA Rule 4370

FINRA is proposing to adopt NASD Rule 3510 (Business Continuity Plans) and NASD Rule 3520 (Emergency Contact Information) into the Consolidated FINRA Rulebook and combine the rules as FINRA Rule 4370 (Business Continuity Plans and Emergency Contact Information). NASD Rule 3510 requires members to create and maintain a written business

¹¹ A "net" transaction is a principal transaction in which a market maker, after having received an order to buy (sell) an equity security, purchases (sells) the equity security at one price (from (to) another broker-dealer or another customer) and then sells to (buys from) the customer at a different price.

¹² See Securities Exchange Act Release No. 54088 (June 30, 2006), 71 FR 38950 (July 10, 2006) (order approving File No. SR-NASD-2004-135).

¹³ See Securities Exchange Act Release No. 38812 (July 3, 1997), 62 FR 37105 (July 10, 1997) (order approving File No. SR-NASD-97-29).

continuity plan identifying procedures relating to an emergency or significant business disruption and enumerates the minimum elements that a member's business continuity plan must address, to the extent those elements are applicable and necessary to the member's business. NASD Rule 3510 further requires members to update their business continuity plans upon any material change and, at a minimum, conduct an annual review of their plans. Each member also must disclose to its customers how its business continuity plan addresses the possibility of a future significant business disruption and how the member plans to respond to events of varying scope. Each member must make this disclosure, at a minimum, in writing to customers at account opening, by posting it on the member's Web site (if the member maintains a Web site), and by mailing it to customers upon request.

NASD Rule 3510 is one part of the NASD Rule 3500 Series (Emergency Preparedness), which requires members to establish emergency preparedness plans and procedures. NASD Rule 3520, which comprises the remainder of the NASD Rule 3500 Series, requires members to designate two emergency contact persons and provide this information to FINRA via electronic process.¹⁴

The Dougherty Letter generally supported the proposal, but recommended one change in the area of emergency contact information. The proposed rule, as is the case today in NASD Rule 3510, originally required that each member report to FINRA two emergency contact persons and that each person be a member of senior management and a registered principal of the

¹⁴ There is no longer a comparable Incorporated NYSE Rule to NASD Rules 3510 and 3520. FINRA previously deleted from the Transitional Rulebook NYSE Rule 446 (Business Continuity and Contingency Plans), which contained substantially similar requirements as the two NASD rules, as part of the rule change to reduce regulatory duplication for Dual Members during the period before completion of the Consolidated FINRA Rulebook. See Securities Exchange Act Release No. 58533 (September 12, 2008), 73 FR 54652 (September 22, 2008) (order approving File No. SR-FINRA-2008-036).

firm.¹⁵ The Dougherty Letter stated that “[t]here may be situations where perhaps the best contact person may not be a registered principal but rather a Financial and Operations Principal or a technology manager.”¹⁶ The Dougherty Letter emphasized that the “purpose of this rule is for FINRA to be able to contact individuals for business continuity purposes.”¹⁷ The commenter pointed out that “the person most knowledgeable on computer systems and business continuity issues may be someone other than a registered principal.”¹⁸

In response, FINRA proposes to revise FINRA Rule 4370 to require that only one of a member’s two designated emergency contact persons must be a member of senior management and a registered principal of the firm.¹⁹ The proposed rule change, however, would require that someone designated as a second emergency contact person who is not a registered principal must be a member of senior management who has knowledge of the member’s business operations.²⁰ The proposed rule change also would clarify that each emergency contact person must be an associated person of the member.²¹ In addition, FINRA proposes to amend FINRA Rule 4370 to codify existing guidance that in the case of a member with only one associated person (e.g., a sole proprietorship without any other associated persons), the second emergency contact person may be an individual, either registered with another firm or nonregistered, who has knowledge of the member’s business operations, such as the member’s attorney, accountant, or clearing firm

¹⁵ See proposed FINRA Rule 4370.

¹⁶ See Dougherty Letter, supra note 4.

¹⁷ Id.

¹⁸ Id.

¹⁹ See Amendment No. 1, supra note 6.

²⁰ Id.

²¹ Id.

contact.²² The Commission believes that transferring and combining NASD Rules 3510 and 3520 into the Consolidated FINRA Rulebook will help ensure that members are prepared in the event of a significant business disruption.

The Commission finds good cause, pursuant to Section 19(b)(2) of the Act,²³ for approving the proposed rule change, as modified, prior to the thirtieth day after the date of publication of notice in the Federal Register. FINRA's proposed changes, with the exception of the proposed revisions contained in Amendment No. 1, were published for comment by the Commission.²⁴ The Commission believes that Amendment No. 1 provides greater clarity regarding the designation of emergency contact persons and is consistent with a purpose of this rule, which is to provide FINRA with a means to contact a member in the event of a significant business disruption.

Accordingly, the Commission finds that there is good cause, consistent with Section 15A(b)(6) of the Act,²⁵ to approve the proposed rule change, as modified by Amendment No. 1, on an accelerated basis.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as modified by Amendment No. 1, is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

²² Id.

²³ 15 U.S.C. 78s(b)(2).

²⁴ FINRA noted that it proposes to announce the implementation date of the proposed rule change in a Regulatory Notice to be published no later than 90 days following Commission approval.

²⁵ 15 U.S.C. 78q-3(b)(6).

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2009-036 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2009-036. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change 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, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2009-036 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²⁶ that the proposed rule change (SR-FINRA-2009-036), as modified by Amendment No. 1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁷

Florence E. Harmon
Deputy Secretary

²⁶ 15 U.S.C. 78s(b)(2).

²⁷ 17 CFR 200.30-3(a)(12).