

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60437; File No. SR-FINRA-2009-052)

August 5, 2009

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change to Adopt FINRA Rule 2264 (Margin Disclosure Statement) in the Consolidated FINRA Rulebook

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on July 29, 2009, Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“SEC” or “Commission”) the proposed rule change as described in Items I, II, and III below, which Items substantially have been prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. *Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change*

FINRA is proposing to adopt NASD Rule 2341 (Margin Disclosure Statement) with minor changes as FINRA Rule 2264 in the consolidated FINRA rulebook.

The text of the proposed rule change is available on FINRA’s Web site at <http://www.finra.org>, at the principal office of FINRA, and at the Commission’s Public Reference Room.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

II. *Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change*

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. *Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change*

1. Purpose

As part of the process of developing a new consolidated rulebook ("Consolidated FINRA Rulebook"),³ FINRA is proposing to adopt NASD Rule 2341 (Margin Disclosure Statement) with minor changes as FINRA Rule 2264 in the Consolidated FINRA Rulebook.

NASD Rule 2341 requires members that open margin accounts for or on behalf of non-institutional customers⁴ to deliver to such customers, prior to or at the time of

³ The current FINRA rulebook consists of (1) FINRA Rules; (2) NASD Rules; and (3) rules incorporated from NYSE ("Incorporated NYSE Rules") (together, the NASD Rules and Incorporated NYSE Rules are referred to as the "Transitional Rulebook"). While the NASD Rules generally apply to all FINRA members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE ("Dual Members"). The FINRA Rules apply to all FINRA members, unless such rules have a more limited application by their terms. For more information about the rulebook consolidation process, see *Information Notice*, March 12, 2008 (Rulebook Consolidation Process).

⁴ For purposes of the rule, a non-institutional customer means a customer that does not qualify as an "institutional account" under NASD Rule 3110(c)(4). NASD rule 3110(c)(4) provides, "the term 'institutional account' shall mean the account of: (A) a bank, savings and loan association, insurance company, or registered investment company; (B) an investment adviser registered either with

opening the account, a specified margin disclosure statement to highlight the risks involved in trading securities in a margin account. Members must disclose that the securities purchased on margin are the firm's collateral for the loan and that, if the securities in the margin account decline in value, the firm can take action, such as issuing a margin call and/or selling securities or other assets in any of the customer's other accounts, to maintain the required equity in the account.

The disclosure statement includes six specific points of information that must be disclosed to non-institutional customers before or at the time a margin account is opened for or on behalf of such customer:

- *You can lose more funds than you deposit in the margin account.* A decline in the value of securities that are purchased on margin may require you to provide additional funds to the firm that has made the loan to avoid the forced sale of those securities or other securities or assets in your account(s).
- *The firm can force the sale of securities or other assets in your account(s).* If the equity in your account falls below the maintenance margin requirements, or the firm's higher "house" requirements, the firm can sell the securities or other assets in any of your accounts held at the firm to cover the margin deficiency. You also will be responsible for any short fall in the account after such a sale.
- *The firm can sell your securities or other assets without contacting you.* Some investors mistakenly believe that a firm must contact them for a margin call to be valid, and that the firm cannot liquidate securities or other assets in their accounts to meet the call unless the firm has contacted them first. This is not the case. Most firms will attempt to notify their customers of margin calls, but they are not required to do so. However, even if a firm has contacted a customer and provided a specific date by which the customer can meet a margin call, the firm can still take necessary steps to protect its financial interests, including immediately selling the securities without notice to the customer.

the Securities and Exchange Commission under Section 203 of the Investment Advisers Act of 1940 or with a state securities commission (or any agency or office performing like functions); or (C) any other entity (whether a natural person, corporation, partnership, trust, or otherwise) with total assets of at least \$50 million." FINRA is proposing to adopt NASD Rule 3110(c)(4) as FINRA Rule 4512(c). *See Regulatory Notice 08-25* (May 2008).

- *You are not entitled to choose which securities or other assets in your account(s) are liquidated or sold to meet a margin call.* Because the securities are collateral for the margin loan, the firm has the right to decide which security to sell in order to protect its interests.
- *The firm can increase its “house” maintenance margin requirements at any time and is not required to provide you advance written notice.* These changes in firm policy often take effect immediately and may result in the issuance of a maintenance margin call. Your failure to satisfy the call may cause the member to liquidate or sell securities in your account(s).
- *You are not entitled to an extension of time on a margin call.* While an extension of time to meet margin requirements may be available to customers under certain conditions, a customer does not have a right to the extension.

Members also must provide the margin disclosure statement (or an abbreviated version as provided by the rule) to non-institutional margin account customers not less than once a calendar year. The rule provides members with the flexibility to use an alternative disclosure statement to the language specified in the rule provided that the alternative disclosures are substantially similar to the disclosures specified in the rule. Members must deliver the initial and annual disclosure statement, in writing or electronically, to customers covered by the rule on an individual basis.

In addition, the rule requires members that permit non-institutional customers to open accounts online, or engage in transactions in securities online, to post the margin disclosure statement on their Web sites in a clear and conspicuous manner. This provision was added to NASD Rule 2341 in 2002 based on a recommendation by the General Accountability Office (GAO) as a means to allow a broader array of persons to review the disclosures.

NASD Rule 2341 was approved by the SEC on April 26, 2001, and was the product of notice and comment rulemaking. FINRA proposes to adopt the requirements set forth in NASD Rule 2341 as FINRA Rule 2264 in the Consolidated FINRA

Rulebook with minor changes. The minor changes, consistent with prior interpretive guidance, clarify that the initial margin disclosure statement may be furnished to customers in a separate document (or contained by itself on a separate page as part of another document), and that the annual disclosure statement may be provided within other documentation, such as the account statement, and does not have to be on a separate page.⁵ In addition, FINRA is proposing a minor change to clarify and update the rule text provisions stating that disclosure statements may be provided to individuals either “in writing or electronically.” Because electronic documents may be considered a form of “writing,” FINRA is proposing to amend the text to state that the documents may be provided “in paper or electronic form.”

FINRA will announce the implementation date of the proposed rule change in a *Regulatory Notice* to be published no later than 90 days following Commission approval.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁶ 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

⁵ In 2001, FINRA issued interpretive guidance that, while the rule requires the initial disclosure statement to be provided in a separate document, the disclosure statement can be provided with or as part of another document provided that it is contained by itself on a separate page. The interpretation also clarified that the annual disclosure statement may be provided within other documentation, such as the account statement, and does not have to be on a separate page. *Regulatory and Compliance Alert* (Summer 2001).

⁶ 15 U.S.C. 78o-3(b)(6).

interest. FINRA believes that the required margin disclosures provide investors with important information with which they can better understand the operation of margin accounts and the risks associated with margin trading.

B. *Self-Regulatory Organization's Statement on Burden on Competition*

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

C. *Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others*

Written comments were neither solicited nor received.

III. *Date of Effectiveness of the Proposed Rule Change 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 self-regulatory organization consents, the Commission will:

(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 change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- 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-2009-052 on the subject line.

Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2009-052. 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 such 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-2009-052 and should be submitted on or before [insert date 21 days from publication in the *Federal Register*].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁷

Florence E. Harmon
Deputy Secretary

⁷ 17 CFR 200.30-3(a)(12).