SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-63196; File No. SR-FINRA-2010-046)

October 27, 2010

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change to Remove the Exemption From the Trading Activity Fee for Transactions in Exchange Listed Options Effected by a Member When FINRA is not the Designated Options Examining Authority for that Member

I. Introduction

On September 7, 2010, Financial Industry Regulatory Authority, Inc. ("FINRA") 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 amend its By-Laws to remove the exemption from the trading activity fee ("TAF") for transactions in exchange listed options effected by a member when FINRA is not the designated options examining authority ("DOEA") for that member. The proposed rule change was published for comment in the Federal Register on September 23, 2010.[3] The Commission received no comment letters on the proposal. This order approves the proposed rule change.

II. Description of the Proposed Rule Change

In its proposal, FINRA sought to amend Section 1(b) of Schedule A to the FINRA By-Laws to remove the exemption from the TAF for transactions in exchange listed options effected by a member for whom FINRA is not the DOEA. The TAF is one of three member regulatory fees FINRA uses to fund its member regulation activities.[4] Because the TAF funds FINRA's

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 See Securities Exchange Act Release No. 62927 (September 17, 2010), 75 FR 58004.

4 See FINRA By-Laws, Schedule A, § 1(b). In addition to the TAF, the other member regulatory fees are the Gross Income Assessment and the Personnel Assessment. See id. §§ 1(c), (d).

member regulation functions, it is intended to apply to transactions in a way that corresponds to FINRA's regulatory responsibilities.[5] In general, the TAF is assessed for the sale of all exchange registered securities wherever executed (except debt securities that are not TRACE-eligible), over-the-counter equity securities, security futures, TRACE-Eligible Securities (provided that the transaction is a Reportable TRACE Transaction), and all municipal securities subject to the reporting requirements of the Municipal Securities Rulemaking Board.[6] The TAF rules also include numerous exemptions for certain types of transactions.[7]

In 2003, FINRA exempted from the TAF "[t]ransactions in exchange listed options effected by a member when FINRA is not the designated options examining authority for that member."[8] FINRA represented that the exemption was added to reflect the fact that FINRA's regulatory responsibilities with respect to such activities were somewhat alleviated by its participation in a plan filed with the Commission under Rule 17d-2 of the Act[9] ("17d-2 Agreement") in which regulatory responsibilities for certain FINRA members that conducted a public options business were assumed by other self regulatory organizations ("SROs") that would act as the members' DOEA.[10] In view of the fact that another SRO performed certain regulatory responsibilities with respect to the options activities of some of its members, FINRA

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5 See Securities Exchange Act Release No. 50485 (October 1, 2004), 69 FR 60445 (October 8, 2004) (SR-NASD-2003-201).

6 See FINRA By-Laws, Schedule A, § 1(b)(1).

7 See FINRA By-Laws, Schedule A, § 1(b)(2).

8 FINRA By-Laws, Schedule A, § 1(b)(2)(K). See Securities Exchange Act Release No. 47946 (May 30, 2003), 68 FR 34021 (June 6, 2003) (SR-NASD-2002-148).

9 17 CFR 240.17d-2.

10 See Securities Exchange Act Release No. 46800 (November 8, 2002), 67 FR 69774 (November 19, 2002).

decided to exempt transactions in exchange listed options by such members from the TAF.[11] The exemption was also based on the fact that certain other SROs were assessing or preparing to assess specific regulatory fees for acting as DOEA,[12] which FINRA believed made its TAF on options transactions appear redundant. However, subsequent amendments to the 17d-2 Agreement have consolidated within FINRA sole regulatory responsibility for the public options activities of all of its members[13] and FINRA assumed all regulatory responsibility for FINRA members under the 17d-2 Agreement.[14] As a result of this increase in regulatory responsibility, FINRA filed the instant proposed rule change to delete the exemption from the TAF.[15]

FINRA represented that deleting this exemption would also remove any ambiguities over whether FINRA should collect the TAF from sole-FINRA members or from FINRA members that conduct only a proprietary options business. FINRA stated its belief that the existing language exempting a member's transactions in exchange listed options from the TAF when FINRA is not the DOEA for the member does not properly align with those situations where

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11 Transactions in over-the-counter ("conventional") options are exempted from the TAF with respect to all FINRA members. See FINRA By-Laws, Schedule A, § 1(b)(2)(H).

12 See, e.g., Securities Exchange Act Release No. 47577 (March 26, 2003), 68 FR 16109 (April 2, 2003) (SR-PCX-2003-03) (PCX rule filing establishing a DOEA fee).

13 See Securities Exchange Act Release No. 57987 (June 18, 2008), 73 FR 36156 (June 25, 2008).

14 Following the consolidation of National Association of Securities Dealers ("NASD") and NYSE member regulation operations in 2007, FINRA announced that it serves as the DOEA for all FINRA member firms. See Regulatory Notice 08-37 (July 2008).

15 At the time FINRA (then NASD) proposed the exemption in Amendment No. 4 to SR-NASD-2002-148, it noted that "NASD does not believe it is precluded from seeking further amendments to the TAF with respect to the reduction or elimination of the proposed exemption . . . in the event of a change of factors surrounding its sales practice and other regulatory responsibilities." Letter from Barbara Z. Sweeney, SVP and Corporate Secretary, NASD, to Katherine A. England, Assistant Director, Division of Trading and Markets, Commission, dated May 19, 2003.

FINRA has regulatory responsibility over the member firm. First, the DOEA designation is established only under the 17d-2 Agreement, which by its own terms applies only with respect to firms that are members of more than one SRO. Thus, according to FINRA, while it has regulatory responsibilities for the options business of its sole members, it is not technically the DOEA for such firms. Second, the 17d-2 Agreement addresses only a firm's public options business. As such, a firm that conducts only a proprietary options business, irrespective of whether such firm is a member of FINRA and another SRO, would not be covered by the 17d-2 Agreement, and FINRA would not technically be the DOEA. FINRA stated that although its regulatory responsibilities are more limited for a firm that does not conduct a public options business, it still retains regulatory responsibilities over the firm's options activities.

III. Discussion and Commission Findings

After carefully reviewing the proposed rule change, the Commission finds that the proposal is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.[16] In particular, the Commission finds that the proposal is consistent with Section 15A(b)(5) of the Act,[17] which requires that a national securities association have rules that provide for the equitable allocation of reasonable dues, fees, and other charges among its members and other persons using its facilities. Further, the Commission finds that the proposal is consistent with Section 15A(b)(6) of the Act,[18] which requires, among other things, that FINRA rules be designed to prevent fraudulent and

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

17 15 U.S.C. 78o-3(b)(5).

18 15 U.S.C. 78o-3(b)(6).

manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

The Commission believes that removal of the TAF exemption for transactions in exchange listed options effected by members for whom FINRA is not the DOEA is consistent with the Act because it more properly aligns the imposition of the TAF with those situations where FINRA has regulatory responsibility over the member firm.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[19] that the proposed rule change (SR-FINRA-2010-046) be, and hereby is, approved.[20]

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[21]

Florence E. Harmon
Deputy Secretary

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19 15 U.S.C. 78s(b)(2).

20 FINRA states it will implement the proposed rule change on the first day of the month following Commission approval. FINRA will announce the implementation of the proposed rule change in a Regulatory Notice to be published no later than 30 days following Commission approval.

21 17 CFR 200.30-3(a)(12).