

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-59962; File No. SR-FINRA-2009-020)

May 21, 2009

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change Relating to the FINRA Regulation Board Composition and Conforming Changes to the FINRA Regulation By-Laws

I. Introduction

On March 27, 2009, 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 amend the By-Laws of FINRA Regulation, Inc. (“FINRA Regulation”) to modify the composition of the board of directors of FINRA Regulation (“FINRA Regulation Board”), to adopt changes to conform the FINRA Regulation By-Laws to the FINRA By-Laws, and to make various non-substantive or conforming changes. The proposed rule change was published for comment in the Federal Register on April 8, 2009.³ The Commission received no comments on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

On July 30, 2007, NASD and New York Stock Exchange Regulation, Inc. (“NYSE Regulation”), the regulatory subsidiary of the New York Stock Exchange, consolidated their member firm regulation operations into a combined organization, FINRA. As part of the consolidation, the Commission approved amendments to the NASD By-Laws to implement

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 59696 (April 2, 2009), 74 FR 16020 (“Notice”).

governance and related changes.⁴ The approved changes included a FINRA Board governance structure that balanced public and industry representation. FINRA Regulation (formerly known as NASD Regulation, Inc. (“NASD Regulation”)) is a subsidiary of FINRA that operates according to the Plan of Allocation and Delegation of Functions by NASD to Subsidiaries, as amended, which NASD adopted in 1996 when it formed NASD Regulation. FINRA Regulation’s By-Laws were not amended at the time of the consolidation, other than in a few sections where those By-Laws conflicted with the new FINRA By-Laws.

The proposed rule change would modify the FINRA Regulation By-Laws to parallel more closely the composition and governance structure of the FINRA board of directors (“FINRA Board”). In addition, the proposed rule change would modify the FINRA Regulation By-Laws to reflect current business and legal practices concerning the administration and capital stock of FINRA Regulation. Furthermore, the proposed rule change would make non-substantive or conforming changes, including updating the FINRA Regulation By-Laws to reflect the corporate name change. A more detailed description of the proposed rule change is provided in the Notice.⁵ The Commission discusses below the most significant aspects of the proposed changes to the FINRA Regulation By-Laws.

III. Discussion and Commission’s Findings

After careful review of the proposed rule change, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations

⁴ See Securities Exchange Act Release No. 56145 (July 26, 2007), 72 FR 42169 (August 1, 2007), as amended by Securities Exchange Act Release No. 56145A (May 30, 2008), 73 FR 32377 (June 6, 2008) (File No. SR-NASD-2007-023) (“Consolidation Approval Order”).

⁵ See supra note 3.

thereunder applicable to a national securities association.⁶ In particular, the Commission finds that the proposed rule change is consistent with the provisions of Section 15A(b)(4) of the Act,⁷ which requires that FINRA rules be designed to assure a fair representation of FINRA's members in the selection of its directors and the administration of its affairs.

The FINRA By-Laws provide that the FINRA Board currently must consist of the Chief Executive Officer of FINRA, the Chief Executive Officer of NYSE Regulation, eleven Public Governors and ten Industry Governors, including a Floor Member Governor, an Independent Dealer/Insurance Affiliate Governor, an Investment Company Affiliate Governor, three Small Firm Governors, one Mid-Size Firm Governor, and three Large-Firm Governors.⁸ The Small Firm Governors, Mid-Size Firm Governor, and Large-Firm Governors are elected by members of FINRA according to their classification as a Small Firm, Mid-Size Firm or Large Firm.⁹

The proposed rule change would provide that the FINRA Regulation Board continue to consist of between 5 and 15 members,¹⁰ and that FINRA Regulation Board members be elected by, and drawn exclusively from, the FINRA Board. Additionally, the proposed rule change would require that the FINRA Regulation Board, like the FINRA Board, have a greater number of Public Directors than Industry Directors.¹¹ In addition, to ensure fair representation on the

⁶ 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).

⁷ 15 U.S.C. 78o-3(b)(4).

⁸ See FINRA By-Laws, Article VII, Section 4 and XXII, Section 2(a).

⁹ See FINRA By-Laws, Article I(z), Article I(dd), Article I(xx) (defining Small Firm Governor, Mid-Size Firm Governor, and Large-Firm Governor), and Article VII, Section 4(a).

¹⁰ See proposed FINRA Regulation By-Laws, Article IV, Section 4.2 (Number of Directors).

¹¹ See proposed FINRA Regulation By-Laws, Article IV, Section 4.3(a) (Qualifications).

FINRA Regulation Board, the proposed rule change also would require that at least two, and not less than 20%, of the Directors of the FINRA Regulation Board be Small, Mid-Size, or Large Firm Governors.¹² The Commission notes that it previously found the composition of the FINRA Board to be consistent with the fair representation requirement of Section 15A(b)(4) of the Act.¹³ The Commission further notes that it has previously found a requirement that at least 20% of directors represent the exchange's members to be consistent with the fair representation requirement applicable to national securities exchanges under Section 6(b)(3) of the Act.¹⁴ Accordingly, the Commission believes that the requirement that the FINRA Regulation Board be composed of at least two, and not less than 20%, of FINRA Regulation's Directors be Small Firm, Mid-Size Firm or Large-Firm Governors is consistent with Section 15A(b)(4) of the Act.

The Commission also finds that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹⁵ 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. The Commission believes that the proposed changes to the FINRA Regulation By-Laws should allow the FINRA Regulation Board to operate in a more effective and efficient manner by, among other things, having a similar composition and a complementary governance structure to the FINRA Board.

¹² See id.

¹³ See Consolidation Approval Order, supra note 4.

¹⁴ See, e.g., Securities Exchange Act Release No. 58324 (August 7, 2008), 73 FR 46936, 46941 (August 12, 2008) (SR-BSE-2008-02, SR-BSE-2008-23, SR-BSE-2008-25, SR-BSECC-2008-01).

¹⁵ 15 U.S.C. 78o-3(b)(6).

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁶ that the proposed rule change (SR-FINRA-2009-020) be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁷

Florence E. Harmon
Deputy Secretary

¹⁶ 15 U.S.C. 78s(b)(2).

¹⁷ 17 CFR 200.30-3(a)(12).