Regulatory Notice 09-72

SEC Approves New Consolidated FINRA Rules

SEC Approval and Effective Dates for New Consolidated FINRA Rules

Effective Date (all rules except FINRA Rule 2330): February 15, 2010

Effective Date (FINRA Rule 2330): February 8, 2010

Executive Summary

Following the consolidation of NASD and the member regulation, enforcement and arbitration functions of NYSE Regulation into FINRA, FINRA established a process to develop a new consolidated rulebook (Consolidated FINRA Rulebook), which FINRA has discussed in previous *Information Notices*.[1] FINRA is proposing new consolidated rules in phases for approval by the SEC as part of the Consolidated FINRA Rulebook.[2] In October and November, the SEC approved eight new consolidated FINRA rules.[3] All of the new rules take effect on February 15, 2010 except for FINRA Rule 2330, which has an implementation date of February 8, 2010.

Questions regarding this *Notice* should be directed to:

- Adam Arkel, Assistant General Counsel, Office of General Counsel (OGC), at (202) 728-6961 (regarding FINRA Rule 2251);
- Lisa Horrigan, Associate General Counsel, OGC, at (202) 728-8190 (regarding FINRA Rule 5290);
- Stan Macel, Assistant General Counsel, OGC, at (202) 728-8056 (regarding FINRA Rules 2130 and 2270);
- Racquel Russell, Assistant General Counsel, OGC, at (202) 728-8363 (regarding FINRA Rules 5210 and 5220);

Financial Industry Regulatory Authority

December 2009

Notice Type

- Consolidated Rulebook
- Rule Approval

Suggested Routing

- Compliance
- Legal
- Operations
- Senior Management

Key Topics

- Approval Procedures for Day-Trading Accounts
- Day-Trading Risk Disclosure Statement
- Forwarding of Proxy and Other Issuer-Related Materials
- Members' Responsibilities Regarding Deferred Variable Annuities
- Offers at Stated Prices
- Order Entry and Execution Practices
- Publication of Transactions and Quotations
- Use of Information Obtained in Fiduciary Capacity

Referenced Rules & Notices

- FINRA Rule 2060
- FINRA Rule 2130
- FINRA Rule 2251
- FINRA Rule 2270
- FINRA Rule 2330
- FINRA Rule 5210
- FINRA Rule 5220
- FINRA Rule 5290
- Information Notice 03/12/08
- Information Notice 10/06/08
- Regulatory Notice 08-57

- Matthew Vitek, Counsel, OGC, at (202) 728-6961 (regarding FINRA Rule 2060); or
- Jim Wrona, Associate Vice President & Associate General Counsel, OGC, at (202) 728-8270 (regarding FINRA Rule 2330).

Background & Discussion

In October and November 2009, the SEC approved eight FINRA rules as part of the Consolidated FINRA Rulebook:

- Rule 2060 (Use of Information Obtained in Fiduciary Capacity);[4]
- Rule 2130 (Approval Procedures for Day-Trading Accounts);[5]
- Rule 2251 (Forwarding of Proxy and Other Issuer-Related Materials);[6]
- Rule 2270 (Day-Trading Risk Disclosure Statement);[7]
- Rule 2330 (Members' Responsibilities Regarding Deferred Variable Annuities);[8]
- Rule 5210 (Publication of Transactions and Quotations);[9]
- Rule 5220 (Offers at Stated Prices);[10] and
- Rule 5290 (Order Entry and Execution Practices).[11]

The attachment to this *Notice* sets forth additional information regarding these new consolidated rules and includes a hyperlink to each related rule filing. The filings provide, among other things, FINRA's statement of the purpose of the rule changes and an exhibit showing the changes between the new rule text and the text of the NASD rule as it exists in the Transitional Rulebook. Also, the text of each new FINRA Rule is available in the online FINRA Manual at *www.finra.org/finramanual*.[12]

Rule Conversion Chart

As discussed in additional detail in *Information Notice 10/06/08* and *Regulatory Notice 08-57*, FINRA has posted three Rule Conversion Charts on its Web site to help firms become familiar with the new rules and show how the new rules relate to the NASD and/or Incorporated NYSE Rules in the Transitional Rulebook that they will replace.

Firms should be aware that the charts are intended as a reference aid only. FINRA reminds firms that the charts do not in any way serve as a substitute for diligent review of the relevant new rule language. The Rule Conversion Charts are located at *www.finra.org/ruleconversionchart*.

Endnotes

1 *See Information Notice 10/06/08* (Rulebook Consolidation Process: Effective Dates of New Consolidated Rules; Introduction of Rule Conversion Chart); *see also Information Notice 03/12/08* (Rulebook Consolidation Process).

2 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 member firms, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (Dual Members). The new FINRA Rules apply to all member firms, unless such rules have a more limited application by their terms. As the Consolidated FINRA Rulebook expands with the SEC's approval and with the new FINRA Rules taking effect, the rules in the Transitional Rulebook that address the same subject matter of regulation will be eliminated. When the Consolidated FINRA Rulebook is completed, the Transitional Rulebook will have been eliminated in its entirety.

3 FINRA Rule 2330 (Members' Responsibilities Regarding Deferred Variable Annuities) was filed for immediate effectiveness pursuant to Section 19(b)(3)(A) of the Exchange Act. *See* discussion of FINRA Rule 2330 in Attachment A.

4 *See* Exchange Act Release No. 61071 (November 30, 2009); 74 FR 64109 (December 7, 2009) (Order Approving Proposed Rule Change; File No. SR-FINRA-2009-067).

5 *See* Exchange Act Release No. 61059 (November 24, 2009); 74 FR 62847 (December 1, 2009) (Order Approving Proposed Rule Change; File No. SR-FINRA-2009-059).

6 *See* Exchange Act Release No. 61052 (November 23, 2009); 74 FR 62857 (December 1, 2009) (Order Approving Proposed Rule Change; File No. SR-FINRA-2009-066).

7 *See supra* note 4.

8 *See* Exchange Act Release No. 61122 (December 7, 2009); 74 FR 65816 (December 11, 2009) (Notice of Filing and Immediate Effective of Proposed Rule Change; File No. SR-FINRA-2009-083).

9 *See* Exchange Act Release No. 60835 (October 16, 2009); 74 FR 54616 (October 22, 2009) (Order Approving Proposed Rule Change; File No. SR-FINRA- 2009-055).

10 *See supra* note 8.

11 *See supra* note 3.

12 FINRA updates the rule text on its online *Manual* within two business days of SEC approval of changes to the rule text.

Attachment A

List of Approved Rules (and Related Rule Filings)

The SEC approved the following new FINRA rules in October and November 2009. The effective date of all of the rules is February 15, 2010, except for Rule 2330 which has an implementation date of February 8, 2010.

FINRA Rule Filing SR-FINRA-2009-055

www.finra.org/rulefilings/2009-055

FINRA Rule 5210

The rule change adopts, without material change, NASD Rule 3310 (Publication of Transactions and Quotations) and NASD IM-3310 (Manipulative and Deceptive Quotations) as FINRA Rule 5210 (Publication of Transactions and Quotations) in the Consolidated FINRA Rulebook.

FINRA Rule 5210 prohibits members from publishing or circulating, or causing to be published or circulated, any communication that purports to report any transaction as a purchase or sale of any security, unless such member believes that such transaction was a bona fide purchase or sale of such security. The rule also prohibits members from publishing or circulating, or causing to be published or circulated, any communication that purports to quote the bid price or asked price for any security, unless the member believes that such quotation represents a bona fide bid for, or offer of, such security.

Supplementary material to FINRA Rule 5210 provides that it would be inconsistent with FINRA Rules 2010 (Standards of Commercial Honor and Principles of Trade), 2020 (Use of Manipulative, Deceptive or Other Fraudulent Devices) and 5210 (Publication of Transactions and Quotations) for a member to publish or circulate or cause to be published or circulated, by any means whatsoever (1) any report of any securities transaction or of any purchase or sale of any security unless such member knows or has reason to believe that such transaction was a bona fide transaction, purchase or sale, or (2) any quotation for any security without having reasonable cause to believe that such quotation is a bona fide quotation, is not fictitious and is not published or circulated or caused to be published or circulated for any fraudulent, deceptive or manipulative purpose.

As further addressed in *Notice to Members (NTM) 04-66*, FINRA reminds members of their obligations under NASD Rule 3010 (Supervision) to have in place a supervisory system and written supervisory procedures reasonably designed to ensure that such orders placed into trading systems are not entered in error or in a manner inconsistent with FINRA rules, including NASD Rule 5210 (Publication of Transactions and Quotations).

FINRA Rule 5220

The rule change adopts, without material change, NASD Rule 3320 (Offers at Stated Prices) and NASD IM-3320 (Firmness of Quotations) as FINRA Rule 5220 (Offers at Stated Prices) in the Consolidated FINRA Rulebook.

FINRA Rule 5220 provides that no member shall make an offer to buy from or sell to any person any security at a stated price unless such member is prepared to purchase or sell, as the case may be, at such price and under such conditions as are stated at the time of such offer to buy or sell.

Supplementary material to FINRA Rule 5220 provides that it shall be deemed conduct inconsistent with high standards of commercial honor and just and equitable principles of trade if a member "backs away" from its quotation. Rule 5220 recognizes that members change inter-dealer quotations constantly in the course of trading, but under normal circumstances where the member is making a firm trading market in any security, it is expected at least to buy or sell a normal unit of trading in the quoted stock at its then-prevailing quotations, unless clearly designated as "not firm" or "firm for less than a normal unit of trading" when supplied by the member. The supplementary material further provides that, if at the time an order for the purchase or sale of the quoted security is presented, the member is in the process of effecting a transaction in such quoted security, and immediately after the completion of such transaction, communicates a revised quotation size, such member shall not be obligated to purchase or sell the quoted security in an amount greater than such revised quotation size.

Rule/Series Number	Rule Title
Rule 5000 Series	**SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES**
Rule 5200 Series	**QUOTATION AND TRADING OBLIGATIONS AND PRACTICES**
Rule 5210	Publication of Transactions and Quotations
Rule 5220	Offers at Stated Prices

FINRA Rule Filing SR-FINRA-2009-059

www.finra.org/rulefilings/2009-059

FINRA Rules 2130 and 2270

The rule change adopts, with certain modifications, NASD Rule 2360 (Approval Procedures for Day-Trading Accounts) as FINRA Rule 2130 (Approval Procedures for Day-Trading Accounts); and NASD Rule 2361 (Day-Trading Risk Disclosure Statement) as FINRA Rule 2270 (Day-Trading Risk Disclosure Statement).

FINRA Rules 2130 and 2270 focus on members' obligations to disclose to non-institutional customers the basic risks of engaging in a day-trading strategy and to assess the appropriateness of day-trading strategies for such customers. FINRA Rule 2130 creates an obligation on members that promote a day-trading strategy regarding account-opening approval procedures for non-institutional customers. FINRA Rule 2270 creates an obligation on such members to disclose to non-institutional customers the unique risks of engaging in a day-trading strategy.

The rule change made minor changes to the previous NASD rules. These changes included adding supplementary materials to clarify the concept of promoting a day-trading strategy based on previous guidance; to codify the process by which a member may submit advertising materials to FINRA's Advertising Department for review and guidance; and to alert members of additional FINRA rules specifically addressing day-trading.

Rule/Series Number	Rule Title
Rule 2000 Series	**DUTIES AND CONFLICTS**
Rule 2100 Series	**TRANSACTIONS WITH CUSTOMERS**
Rule 2130	Approval Procedures for Day-Trading Accounts
Rule 2200 Series	**COMMUNICATIONS AND DISCLOSURES**
Rule 2260 Series	**DISCLOSURES**
Rule 2270	Day-Trading Risk Disclosure Statement

FINRA Rule Filing SR-FINRA-2009-066

www.finra.org/rulefilings/2009-066

FINRA Rule 2251

The rule change adopts, without material change, NASD Rule 2260 (Forwarding of Proxy and Other Materials) and NASD IM-2260 (Approved Rates of Reimbursement) as FINRA Rule 2251 (Forwarding of Proxy and Other Issuer-Related Materials) in the Consolidated FINRA Rulebook. The rule change makes minor clarifying changes and other changes primarily to reflect the new formatting and terminology conventions of the Consolidated FINRA Rulebook.

FINRA Rule 2251 sets forth certain requirements with respect to the transmission of proxy materials and other communications to beneficial owners of securities and the limited circumstances in which members are permitted to vote proxies without instructions from those beneficial owners. The rule generally requires that a member must, in connection with an equity security, forward promptly or, in connection with a debt security, make reasonable efforts to forward promptly certain information to the beneficial owner, or the beneficial owner's designated investor adviser, if the member carries the account in which the security is held for the beneficial owner and the security is registered in a name other than the name of the beneficial owner. The rule prohibits a member from giving a proxy to vote stock that is registered in its name, unless the member is the beneficial owner of the stock. (The rule sets forth certain exceptions. For example, FINRA Rule 2251(c)(2) provides that a member may give a proxy to vote any stock pursuant to the rules of any national securities exchange of which it is a member provided that the records of the member clearly indicate the procedure it is following.)

The supplementary material to FINRA Rule 2251 regulates the reimbursement that members are entitled to receive in connection with forwarding proxy materials and other communications.

Rule/Series Number	Rule Title
Rule 2200 Series	**COMMUNICATIONS AND DISCLOSURES**
Rule 2250 Series	**PROXY MATERIALS**
Rule 2251	Forwarding of Proxy and Other Issuer-Related Materials

FINRA Rule Filing SR-FINRA-2009-067

www.finra.org/rulefilings/2009-067

FINRA Rule 2060

The rule change adopts, without material change, NASD Rule 3120 (Use of Information Obtained in Fiduciary Capacity) as FINRA Rule 2060 (Use of Information Obtained in Fiduciary Capacity); and NASD Rule 3380 (Order Entry and Execution Practices) as FINRA Rule 5290 (Order Entry and Execution Practices).

FINRA Rule 2060 provides that a member that receives information as to the ownership of securities while acting in the capacity of paying agent, transfer agent, trustee or otherwise shall under no circumstances make use of the information for soliciting purchases, sales or exchanges except at the request and on behalf of the issuer.

FINRA Rule 5290

FINRA Rule 5290 prohibits members and associated persons from splitting any order into multiple smaller orders for execution or any execution into multiple smaller executions for transaction reporting for the primary purpose of maximizing a monetary or in-kind payment to the member or associated persons as a result of the execution of such orders or the transaction reporting of such executions. This is commonly also referred to as "trade shredding," which is the unlawful practice of splitting customer orders for securities into multiple smaller orders for the primary purpose of maximizing payments or rebates to the member.

Rule/Series Number	Rule Title
Rule 2000 Series	**DUTIES AND CONFLICTS**
Rule 2060	Use of Information Obtained in Fiduciary Capacity
Rule 5000 Series	**SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES**
Rule 5200 Series	**QUOTATION AND TRADING OBLIGATIONS AND PRACTICES**
Rule 5290	Order Entry and Execution Practices

FINRA Rule Filing SR-FINRA-2009-083

www.finra.org/rulefilings/2009-083

The rule change—which FINRA filed with the SEC for immediate effectiveness on November 20, 2009, with an implementation date of February 8, 2010—adopts (without material change) NASD Rule 2821 (Members' Responsibilities Regarding Deferred Variable Annuities) as FINRA Rule 2330 (Members' Responsibilities Regarding Deferred Variable Annuities) in the Consolidated FINRA Rulebook. FINRA Rule 2330 establishes sales practice standards for recommended purchases and exchanges of deferred variable annuities. The rule has six main sections. First, it addresses general considerations, such as the rule's applicability. Second, the rule has requirements governing broker recommendations, including suitability and disclosure obligations. Third, the rule includes various principal review and approval obligations. Fourth, the rule requires members to establish and maintain supervisory procedures reasonably designed to achieve compliance with the standards set forth in the rule. Fifth, the rule has a training component. And sixth, the rule has a supplementary material section that addresses a variety of issues, ranging from the handling of customer funds and checks to information gathering and sharing.

Rule/Series Number	Rule Title
Rule 2000 Series	**DUTIES AND CONFLICTS**
Rule 2300 Series	**SPECIAL PRODUCTS**
Rule 2330	Members' Responsibilities Regarding Deferred Variable Annuities