

SEC Approves New Consolidated FINRA Rules

SEC Approval and Effective Date for New Consolidated FINRA Rules

Effective Date: December 15, 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 Securities and Exchange Commission (SEC) as part of the Consolidated FINRA Rulebook.²

In August and September 2010, the SEC approved three rule filings relating to the Consolidated FINRA Rulebook. FINRA Rule 5121 (Public Offerings of Securities With Conflicts of Interest) and the FINRA Rule 11000 Series (Uniform Practice Code) will take effect on December 15, 2010. The effective date of FINRA Rule 3270 (Outside Business Activities of Registered Persons) is also December 15, 2010; however, for registered persons who are actively engaged in an outside business activity prior to December 15, 2010, firms have until June 15, 2011, to review such pre-existing activities under the standards set forth in FINRA Rule 3270, including the requirement that firms keep a record of their compliance with such standards.

October 2010

Notice Type

- Consolidated Rulebook
- Rule Approvals

Suggested Routing

- Compliance
- Legal
- Operations
- Senior Management

Key Topic(s)

- Effective Dates of Consolidated Rules
- FINRA Manual
- Rulebook Consolidation
- Outside Business Activities
- Public Offerings
- Uniform Practice Code

Referenced Rules & Notices

- FINRA Rule 3270
- FINRA Rule 5121
- FINRA Rule 11000 Series
- Information Notice 03/12/08
- Information Notice 10/06/08
- Regulatory Notice 08-57

Questions regarding this *Notice* should be directed to:

- ▶ Kosha Dalal, Associate Vice President and Associate General Counsel, Office of General Counsel (OGC), at (202) 728-6903 (regarding the FINRA Rule 11000 Series);
- ▶ Gary Goldsholle, Vice President and Associate General Counsel, OGC, at (202) 728-8104 (regarding FINRA Rule 3270); or
- ▶ Stan Macel, Assistant General Counsel, OGC, at (202) 728-8056 (regarding FINRA Rule 5121).

Discussion

In August and September 2010, the SEC approved the following new consolidated FINRA Rules as part of the Consolidated FINRA Rulebook:

- ▶ Rule 3270 (Outside Business Activities of Registered Persons)³
- ▶ Rule 5121 (Public Offerings of Securities With Conflicts of Interest)⁴
- ▶ Rule 11000 Series (Uniform Practice Code)⁵

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 the new FINRA rule is available in the online *FINRA Manual* at www.finra.org/finramanual.⁶

Rule Conversion Charts

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 website 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 See Exchange Act Release No. 62762 (Aug. 23, 2010), 75 FR 53362 (Aug. 31, 2010) (Order Approving Proposed Rule Change; File No. SR-FINRA-2009-042).
- 4 See Exchange Act Release No. 62702 (Aug. 12, 2010), 75 FR 51147 (Aug. 18, 2010) (Order Approving Proposed Rule Change; File No. SR-FINRA-2010-026).
- 5 See Exchange Act Release No. 62842 (Sept. 3, 2010), 75 FR 55842 (Sept. 14, 2010) (Order Approving Proposed Rule Change; File No. SR-FINRA-2010-030).
- 6 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 FINRA Rules (and Related Rule Filings)

The SEC approved the following rule filings relating to the Consolidated FINRA Rulebook in August and September 2010. The effective date for FINRA Rule 5121 (Public Offerings of Securities With Conflicts of Interest) and the FINRA Rule 11000 Series (Uniform Practice Code) is December 15, 2010. The effective date of FINRA Rule 3270 (Outside Business Activities of Registered Persons) is also December 15, 2010; however, for registered persons who are actively engaged in an outside business activity prior to December 15, 2010, firms have until June 15, 2011, to review such pre-existing activities under the standards set forth in FINRA Rule 3270, including the requirement that firms keep a record of their compliance with such standards.

FINRA Rule Filing SR-FINRA-2009-042

www.finra.org/rulefilings/2009-042

The rule change adopts, with certain modifications, NASD Rule 3030 (Outside Business Activities of an Associated Person) as FINRA Rule 3270 (Outside Business Activities of Registered Persons) in the Consolidated FINRA Rulebook, and deletes Incorporated NYSE Rule 346 (Limitations – Employment and Association with Members and Member Organizations) and its Interpretation.

FINRA Rule 3270 prohibits any registered person from being an employee, independent contractor, sole proprietor, officer, director or partner of another person, or being compensated, or having the reasonable expectation of compensation, from another person as a result of any business activity outside the scope of the relationship with his or her member firm, unless he or she has provided prior written notice to the firm in the form specified by the firm. Passive investments and activities subject to the requirements of NASD Rule 3040 are exempted from this requirement.

Supplementary Material .01 (Obligations of Member Receiving Notice) to FINRA Rule 3270 sets forth the obligations of a member upon receipt of a written notice of a proposed outside business activity. FINRA Rule 3270 requires that, upon receipt of a written notice, a firm must consider whether the proposed activity will: (1) interfere with or otherwise compromise the registered person's responsibilities to the firm and/or the firm's customers or (2) be viewed by customers or the public as part of the firm's business based upon, among other factors, the nature of the proposed activity and the manner in which it will be offered. Additionally, based on the firm's review of such factors, the firm must evaluate the advisability of imposing specific conditions or limitations on a registered person's outside business activity, including where circumstances warrant, prohibiting the activity. A firm also must evaluate the proposed activity to determine whether the activity properly is characterized as an outside business activity or whether it should be treated as an outside securities activity

subject to the requirements of NASD Rule 3040. A firm must keep a record of its compliance with these obligations with respect to each written notice received and must preserve this record for the period of time and accessibility specified in Exchange Act Rule 17a-4(e)(1).

| Rule/Series No. | Rule Title |
|------------------------|---|
| Rule 3000 Series | SUPERVISION AND RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS |
| Rule 3200 Series | RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS |
| Rule 3270 | Outside Business Activities of Registered Persons |

FINRA Rule Filing SR-FINRA-2010-026

www.finra.org/rulefilings/2010-026

The rule change adopts NASD Rule 2720 (Public Offerings of Securities With Conflicts of Interest) as FINRA Rule 5121 in the Consolidated FINRA Rulebook.

Rule 5121 governs public offerings of securities in which a firm with a conflict of interest participates. It generally prohibits a firm with a “conflict of interest,” as defined in the rule, from participating in a public offering, unless certain other requirements are met. Such requirements include prominent disclosure of the nature of the conflict, and in certain circumstances, the participation of a qualified independent underwriter. Firms also must comply with certain net capital, discretionary accounts and filing requirements, as applicable.

| Rule/Series No. | Rule Title |
|------------------------|---|
| Rule 5000 Series | SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES |
| Rule 5100 Series | SECURITIES OFFERINGS, UNDERWRITING AND COMPENSATION |
| Rule 5120 Series | Offerings of Members’ Securities |
| Rule 5121 | Public Offerings of Securities With Conflicts of Interest |

FINRA Rule Filing SR-FINRA-2010-030

www.finra.org/rulefilings/2010-030

The rule change adopts NASD Rule 11000 Series (Uniform Practice Code (UPC)), with certain changes, as FINRA Rule 11000 Series in the Consolidated FINRA Rulebook. The rule change also deletes NASD Rule 3370 (Purchases) and the following corresponding provisions in the Incorporated NYSE Rules and Interpretations:

- 176 (Delivery Time);
- 180 (Failure to Deliver);
- 282 (Buy-in Procedures) and its Supplementary Material paragraphs .10 - .80; 291 (Failure to Fulfill Closing Contract);
- 292 (Restrictions on Members' Participation in Transaction to Close Defaulted Contracts);
- 293 (Closing Contracts in Suspended Securities);
- 294 (Default in Loan of Money);
- 387 (COD Orders) and its Supplementary Material paragraphs .10 - .60;
- Rule 387 Interpretations /01 - /18; 430 (Partial Delivery of Securities to Customers on C.O.D. Purchases); and
- Rule 430 Interpretation /01.

The UPC prescribes the manner in which over-the-counter securities transactions other than those cleared through a registered clearing agency are compared, cleared and settled between member firms. As a general matter, the UPC does not apply to:

- transactions in securities between firms that are compared, cleared or settled through the facilities of a registered clearing agency, except to the extent that the rules of the clearing agency provide that rules of other organizations shall apply;
- transactions in securities exempted under Section 3(a)(12) of the Exchange Act or municipal securities as defined in Section 3(a)(29) of the Exchange Act;
- transactions in redeemable securities issued by companies registered under the Investment Company Act of 1940, except for secondary market transactions between members in unit investment trusts; and
- transactions in Direct Participation Program securities, except as otherwise provided in the UPC.

Much of the NASD Rule 11000 Series has been transferred with minor changes into the Consolidated FINRA Rulebook, to update certain references and terminology.¹ FINRA Rules 11111 (Refusal to Abide by Rulings of the Committee) and 11112 (Review by Panels of the UPC Committee) consolidate and clarify the scope of reviews by the UPC Committee. FINRA Rules 11820 (Selling-Out), 11860 (COD Orders), 11810 (Buying-In) and 11810.03 (Sample Buy-In Forms) harmonize the differences between the corresponding NYSE rules and the NASD rules and update certain procedures and time frames. New FINRA Rule 11810(b)(4) (Notice of “Buy-In” and Confirmation of Receipt) provides that a seller that receives notice of a “buy-in” must reject it in the manner and time frame provided or will be deemed to have accepted such notice.

FINRA Rules 11870 (Customer Account Transfer Contracts) and 11870.03 (Sample Transfer Instruction Forms) incorporate certain guidance from NYSE Rule 412 (Customer Account Transfer Contracts).²

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- 1 NASD Rules 11890 (Clearly Erroneous Transactions), IM-11890-1 (Refusal to Abide by Rulings) and IM-11890-2 (Review by Panels of the UPC Committee) were adopted, with significant changes, into the Consolidated FINRA Rulebook as the FINRA Rule 11890 Series (Clearly Erroneous Transactions) pursuant to a separate rule filing and were not addressed as part of this rule filing. *See* Exchange Act Release No. 61080 (Dec. 1, 2009), 74 FR 64117 (Dec. 7, 2009) (Order Approving Proposed Rule Change; File No. SR-FINRA-2009-068).
 - 2 FINRA eliminated NYSE Rule 412 and its interpretations from the Transitional Rulebook as part of a rule change to reduce regulatory duplication for Dual Members during the period before completion of the Consolidated FINRA Rulebook. *See* Exchange Act Release No. 58533 (Sept. 12, 2008), 73 FR 54652 (Sept. 22, 2008) (Order Approving Proposed Rule Change; File No. SR-FINRA-2008-036). The NYSE subsequently amended its version of NYSE Rule 412 to state that NYSE members and member organizations shall comply with NASD Rule 11870, concerning the transfer of customer accounts between members, and any amendments thereto, as if such rule is part of the NYSE’s rules.

| Rule/Series No. | Rule Title |
|--------------------------|--|
| Rule 11000 Series | UNIFORM PRACTICE CODE (“UPC”) |
| Rule 11100 | Scope of Uniform Practice Code |
| Rule 11110 | Committees |
| Rule 11111 | Refusal to Abide by Rulings of the Committee |
| Rule 11112 | Review by Panels of the UPC Committee |
| Rule 11120 | Definitions |
| Rule 11121 | Trade Date |
| Rule 11130 | When, As and If Issued/Distributed Contracts |
| Rule 11140 | Transactions in Securities “Ex-Dividend,” “Ex-Rights” or “Ex-Warrants” |
| Rule 11150 | Transactions “Ex-Interest” in Bonds Which Are Dealt in “Flat” |
| Rule 11160 | “Ex” Liquidating Payments |
| Rule 11170 | Transactions in “Part-Redeemed” Bonds |
| Rule 11190 | Reconfirmation and Pricing Service Participants |
| Rule 11200 Series | COMPARISONS OR CONFIRMATIONS AND “DON’T KNOW NOTICES” |
| Rule 11210 | Sent by Each Party |
| Rule 11220 | Description of Securities |
| Rule 11300 Series | DELIVERY OF SECURITIES |
| Rule 11310 | Book-Entry Settlement |
| Rule 11320 | Dates of Delivery |
| Rule 11330 | Payment |
| Rule 11340 | Stamp Taxes |
| Rule 11350 | Part Delivery |
| Rule 11360 | Units of Delivery |
| Rule 11361 | Units of Delivery — Stocks |
| Rule 11362 | Units of Delivery — Bonds |
| Rule 11363 | Units of Delivery — Unit Investment Trust Securities |
| Rule 11364 | Units of Delivery — Certificates of Deposit for Bonds |
| Rule 11365 | Trading Securities As “Units” or Bonds “With Stock” |
| Rule 11400 Series | DELIVERY OF SECURITIES WITH DRAFT ATTACHED |
| Rule 11410 | Acceptance of Draft |

| Rule/Series No. | Rule Title |
|--------------------------|---|
| Rule 11500 Series | DELIVERY OF SECURITIES WITH RESTRICTIONS |
| Rule 11510 | Delivery of Temporary Certificates |
| Rule 11520 | Delivery of Mutilated Securities |
| Rule 11530 | Delivery of Securities Called for Redemption or Which Are Deemed Worthless |
| Rule 11540 | Delivery Under Government Regulations |
| Rule 11550 | Assignments and Powers of Substitution; Delivery of Registered Securities |
| Rule 11560 | Certificate of Company Whose Transfer Books Are Closed |
| Rule 11570 | Certificates in Various Names |
| Rule 11571 | Certificate in Name of Corporation |
| Rule 11572 | Certificate in Name of Firm |
| Rule 11573 | Certificate in Name of Dissolved Firm Succeeded by New Firm |
| Rule 11574 | Certificate in Name of Deceased Person, Trustee, etc. |
| Rule 11580 | Transfer of Limited Partnership Securities |
| Rule 11581 | Limited Partnership Transfer Forms |
| Rule 11600 Series | DELIVERY OF BONDS AND OTHER EVIDENCES OF INDEBTEDNESS |
| Rule 11610 | Liability for Expenses |
| Rule 11620 | Computation of Interest |
| Rule 11630 | Due-Bills and Due-Bill Checks |
| Rule 11640 | Claims for Dividends, Rights, Interest, etc. |
| Rule 11650 | Transfer Fees |
| Rule 11700 Series | RECLAMATIONS AND REJECTIONS |
| Rule 11710 | General Provisions |
| Rule 11720 | Irregular Delivery — Transfer Refused — Lost or Stolen Securities |
| Rule 11721 | Obligations of Members Who Discover Securities in Their Possession to Which They Are Not Entitled |
| Rule 11730 | Called Securities |
| Rule 11740 | Marking to the Market |
| Rule 11800 Series | CLOSE OUT PROCEDURES |
| Rule 11810 | Buy-In Procedures and Requirements |
| Rule 11820 | Selling-Out |
| Rule 11830 | Reserved |
| Rule 11840 | Rights and Warrants |
| Rule 11860 | COD Orders |
| Rule 11870 | Customer Account Transfer Contracts |
| Rule 11880 | Settlement of Syndicate Accounts |
| Rule 11900 | Clearance of Corporate Debt Securities |