

OMB APPROVAL

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Required fields are shown with yellow backgrounds and asterisks.

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SECURITIES AND EXCHANGE COMMISSION
 WASHINGTON, D.C. 20549
 Form 19b-4

File No.* SR - 2009 - * 090

Amendment No. (req. for Amendments *) 1

Proposed Rule Change by Financial Industry Regulatory Authority
 Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934

Initial * ☐ Amendment * ☒ Withdrawal ☐

Section 19(b)(2) * ☒ Section 19(b)(3)(A) * ☐ Section 19(b)(3)(B) * ☐

Rule

Pilot ☐ Extension of Time Period
 for Commission Action * ☐ Date Expires *

☐ 19b-4(f)(1) ☐ 19b-4(f)(4)
☐ 19b-4(f)(2) ☐ 19b-4(f)(5)
☐ 19b-4(f)(3) ☐ 19b-4(f)(6)

Exhibit 2 Sent As Paper Document ☐

Exhibit 3 Sent As Paper Document ☐

Description

Provide a brief description of the proposed rule change (limit 250 characters, required when Initial is checked *).

Contact Information

Provide the name, telephone number and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the proposed rule change.

First Name * Racquel Last Name * Russell
 Title * Assistant General Counsel
 E-mail * racquel.russell@finra.org
 Telephone * (202) 728-8363 Fax (202) 728-8264

Signature

Pursuant to the requirements of the Securities Exchange Act of 1934,

has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized officer.

Date 01/24/2011

By Stephanie M. Dumont
 (Name *)

Senior Vice President and Director of Capital Markets
 Policy

(Title *)

NOTE: Clicking the button at right will digitally sign and lock
 this form. A digital signature is as legally binding as a physical
 signature, and once signed, this form cannot be changed.

Stephanie Dumont,

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EDFS website.

Form 19b-4 Information (required)

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

Exhibit 1 - Notice of Proposed Rule Change (required)

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications

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Exhibit Sent As Paper Document

☐

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

Exhibit 3 - Form, Report, or Questionnaire

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Exhibit Sent As Paper Document

☐

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

Exhibit 4 - Marked Copies

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

Exhibit 5 - Proposed Rule Text

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

Partial Amendment

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

On December 10, 2009, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), SR-FINRA-2009-090, a proposed rule change to adopt NASD Interpretive Material (IM) 2110-2 (Trading Ahead of Customer Limit Order) and NASD Rule 2111 (Trading Ahead of Customer Market Orders) with significant changes in the Consolidated FINRA Rulebook as new FINRA Rule 5320 (“Prohibition Against Trading Ahead of Customer Orders” or the “Rule”). The SEC published the proposed rule change for notice and comment on December 22, 2009¹ and received four comment letters.² FINRA responded to comments on August 31, 2010.³

FINRA is filing this Partial Amendment No. 1 to further address certain issues and make several non-substantive, technical changes to the rule text. First, one commenter raised concerns regarding, among other things, the operation of the Rule during extended hours trading in foreign securities.⁴ This commenter stated that application of the Rule during extended hours may be particularly onerous for firms that execute transactions in foreign securities because of the fluctuations in U.S. and non-U.S. currency exchange rates.⁵ This commenter offered, as an example, a situation where a member places a proprietary order for a foreign security at a price that would not trigger order protection for a customer limit order.⁶ However, due to currency fluctuations since

¹ See Securities Exchange Act Release No. 61168 (December 15, 2009), 74 FR 68084 (December 22, 2009) (Notice of Filing of File No. SR-FINRA-2009-090).

² Letter from Patrick Chi, Chief Compliance Officer, ITG Inc., to Elizabeth M. Murphy, Secretary, SEC, dated January 12, 2010 (“ITG”); Letter from R. Cromwell Coulson, Chief Executive Officer, Pink OTC Markets Inc., to Elizabeth M. Murphy, Secretary, SEC, dated January 18, 2010 (“Pink”); Letter from Ann Vlcek, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association, to Elizabeth M. Murphy, Secretary, SEC, dated January 28, 2010 (“SIFMA”); and Letter from Leonard J. Amoruso, General Counsel, Knight Capital Group, Inc., and Michael T. Corrao, Chief Compliance Officer, Knight Equity Markets, L.P., to Elizabeth M. Murphy, Secretary, SEC, dated February 22, 2010 (“Knight”) (available at <http://www.sec.gov/comments/sr-finra-2009-090/finra2009090.shtml>).

³ A summary of comments and FINRA’s responses thereto are set forth in FINRA’s letter responding to comments regarding the proposed rule change. See FINRA Response to Comments, dated August 31, 2010 (File No. SR-FINRA-2009-090) (“Response to Comments”).

⁴ See SIFMA letter.

⁵ Id.

⁶ Id.

order entry, the member receives an execution at a price (in U.S. dollars) that would trigger a customer limit order.⁷

FINRA is further clarifying its views with respect to compliance with the Rule when trading in foreign securities. In FINRA's Response to Comments, FINRA stated that, if a member executes a trade for its own account in an extended hours session at a price that would satisfy an executable customer order, the Rule would require that the customer's order be executed. FINRA further stated that FINRA would look to the member to demonstrate that, at the time of the execution of the proprietary order, the market and currency conversion information available made it reasonable to conclude that, but for any future fluctuations in currency conversion rates, the trade was not at a price that would trigger the Rule.

FINRA is clarifying that, as is the case during regular trading hours, during extended hours trading the Rule generally would continue to require that members fill executable customer orders whenever the member executes a proprietary transaction at a price that would satisfy the customer's order (or at a price that does not satisfy the customer limit order but does not provide the minimum level of price improvement). The price at which the proprietary transaction is executed, not the price of the proprietary order, is relevant in determining whether the customer order protection requirement has been triggered. Therefore, if a member receives an execution in a foreign security at a price (in U.S. dollars) that would satisfy a customer's order, the member must immediately thereafter execute the customer order up to the size and at the same or better price at which it traded for its own account. FINRA continues to believe that the Rule should apply at all times that a customer order is executable by the member and is not proposing an amendment to this provision.

Second, commenters generally opposed the requirement that members use a separate MPID for a walled-off market making desk. Commenters argued, among other things, that separate MPIDs could pose considerable administrative burdens for firms, making regulatory reporting requirements, such as to FINRA's Order Audit Trail System and Trade Reporting Facility, more complex and expensive. Upon further consideration and in response to commenters' concerns, FINRA has determined to delete the requirement that a member that structures its order handling practices in NMS stocks⁸ to permit its market making desk to trade at prices that would satisfy customer orders held at a separate trading unit assign and use a unique MPID for such market-making desk. FINRA intends to examine alternative means of achieving the objective of the proposed requirement.

FINRA is addressing the applicability of interpretive guidance previously issued in connection with NASD IM-2110-2 and NASD Rule 2111 (e.g., NASD Notices to

⁷ Id.

⁸ Rule 600(b)(47) of SEC Regulation NMS.

Members) to new FINRA Rule 5320. Specifically, consistent with existing policy, where a provision of new FINRA Rule 5320 is not substantively different from NASD IM-2110-2 or NASD Rule 2111, previously issued interpretations generally will continue to apply (unless rescinded or updated by FINRA).

Finally, FINRA also is making certain non-substantive, technical changes to the rule text in this Partial Amendment No. 1. FINRA is including with this Partial Amendment an Exhibit 4 that shows the changes from the originally proposed rule text. Exhibit 5 shows the changes from the current rulebook. Proposed additions are underlined and proposed deletions are bracketed.

EXHIBIT 4

Exhibit 4 shows the changes in this Partial Amendment No. 1, with the changes proposed in the original filing shown as if adopted. Proposed amendments in this Partial Amendment No. 1 appear underlined; proposed deletions appear in brackets.

* * * * *

Text of Proposed New FINRA Rule

* * * * *

5000. SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES

* * * * *

5300. HANDLING OF CUSTOMER ORDERS

5320. Prohibition Against Trading Ahead of Customer Orders

(a) through (b) No Change.

• • • Supplementary Material:-----

.01 No Change.

.02 No-Knowledge Exception

(a) With respect to NMS stocks, as defined in Rule 600 of SEC Regulation NMS, if a member implements and utilizes an effective system of internal controls, such as appropriate information barriers, that operate to prevent one trading unit from obtaining knowledge of customer orders held [at] by a separate trading unit, those other trading units trading in a proprietary capacity may continue to trade at prices that would satisfy the customer orders held by the separate trading unit. A member that structures its order handling practices in NMS stocks to permit its market-making desk to trade at prices that would satisfy customer orders held [at] by a separate trading unit must [(1) assign and use

a unique market participant identifier (MPID) for the market-making desk; and (2)] disclose in writing to its customers, at account opening and annually thereafter, a description of the manner in which customer orders are handled by the member and the circumstances under which the member may trade proprietarily at its market-making desk at prices that would satisfy the customer order.

(b) With respect to OTC equity securities, as defined in Rule 6420, if a member implements and utilizes an effective system of internal controls, such as appropriate information barriers, that operate to prevent a non-market-making trading unit from obtaining knowledge of customer orders held [at] by a separate trading unit, the non-market-making trading unit trading in a proprietary capacity may continue to trade at prices that would satisfy the customer orders held by the separate trading unit.

.03 Riskless Principal Exception. The obligations under this Rule shall not apply to a member's proprietary trade if such proprietary trade is for the purposes of facilitating the execution, on a riskless principal basis, of an[other] order from a customer (whether its own customer or the customer of another broker-dealer) (the "facilitated order"), provided that the member:

(a) No Change.

(b) [the member] has written policies and procedures to ensure that riskless principal transactions [relied] for which the member is relying upon [for] this exception comply with applicable FINRA rules. At a minimum these policies and procedures must require that the customer order was received prior to the offsetting principal transaction, and that the offsetting principal transaction is at the same price as the customer order exclusive of any markup or markdown, commission equivalent or other fee and is

allocated to a riskless principal or customer account in a consistent manner and within 60 seconds of execution.

Members must have supervisory systems in place that produce records that enable the member and FINRA to reconstruct accurately, readily, and in a time-sequenced manner all facilitated orders [on] for which [a] the member relies [in claiming] on this exception.

.04 through .05 No Change.

.06 Minimum Price Improvement Standards. The minimum amount of price improvement necessary for a member to execute an order on a proprietary basis when holding an unexecuted limit order in that same security, and not be required to execute the held limit order is as follows:

(a) No Change.

(b) For customer limit orders priced greater than or equal to \$0.01 and less than \$1.00, the minimum amount of price improvement required is the lesser of \$0.01 or one-half (1/2) of the current inside spread;

(c) For customer limit orders priced less than \$0.01 but greater than or equal to \$0.001, the minimum amount of price improvement required is the lesser of \$0.001 or one-half (1/2) of the current inside spread;

(d) For customer limit orders priced less than \$0.001 but greater than or equal to \$0.0001, the minimum amount of price improvement required is the lesser of \$0.0001 or one-half (1/2) of the current inside spread;

(e) For customer limit orders priced less than \$0.0001 but greater than or equal to \$0.00001, the minimum amount of price improvement required is the lesser of \$0.00001 or one-half (1/2) of the current inside spread;

(f) For customer limit orders priced less than \$0.00001, the minimum amount of price improvement required is the lesser of \$0.000001 or one-half (1/2) of the current inside spread; and

(g) For customer limit orders priced outside the best inside market, the minimum amount of price improvement required must either meet the requirements set forth above or the member must trade at a price at or inside the best inside market for the security.

For purposes of determining the minimum price improvement standards for customer limit orders in OTC equity securities priced below \$1.00 where there is no published current inside spread, members may calculate a current inside spread by contacting and obtaining priced quotations from at least two unaffiliated dealers and using the highest bid and lowest offer obtained in calculating the current inside spread. Where there is only a one-sided quote in an OTC equity security priced below \$1.00, members may calculate the current inside spread by contacting and obtaining priced quotations from at least two unaffiliated dealers and using the best price obtained on the other side of the quote. Members must document the name of each dealer contacted and the quotations received for purposes of determining the current inside spread.

In addition, if the minimum price improvement standards above would trigger the protection of a pending customer limit order, any better-priced customer limit order(s) must also be protected under this Rule, even if those better-priced limit orders would not be directly triggered under the minimum price[-] improvement standards above.

.07 No Change.

.08 Trading Outside Normal Market Hours. Members generally may limit the life of a customer order to the period of normal market hours of 9:30 a.m. to 4:00 p.m. Eastern Time. However, if the customer and member agree to the processing of the customer's order outside normal market hours, the protections of this Rule shall apply to that customer's order(s) at all times the customer order is executable by the member.

* * * * *

EXHIBIT 5

Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

Text of Proposed New FINRA Rule

* * * * *

5000. SECURITIES OFFERING AND TRADING STANDARDS AND PRACTICES

* * * * *

5300. HANDLING OF CUSTOMER ORDERS

5320. Prohibition Against Trading Ahead of Customer Orders

(a) Except as provided herein, a member that accepts and holds an order in an equity security from its own customer or a customer of another broker-dealer without immediately executing the order is prohibited from trading that security on the same side of the market for its own account at a price that would satisfy the customer order, unless it immediately thereafter executes the customer order up to the size and at the same or better price at which it traded for its own account.

(b) A member must have a written methodology in place governing the execution and priority of all pending orders that is consistent with the requirements of this Rule and NASD Rule 2320. A member also must ensure that this methodology is consistently applied.

• • • Supplementary Material:-----

.01 Large Orders and Institutional Account Exceptions. With respect to orders for customer accounts that meet the definition of an “institutional account” as defined in

NASD Rule 3110, or for orders of 10,000 shares or more (unless such orders are less than \$100,000 in value), a member is permitted to trade a security on the same side of the market for its own account at a price that would satisfy such customer order, provided that the member has provided clear and comprehensive written disclosure to such customer at account opening and annually thereafter that:

(a) discloses that the member may trade proprietarily at prices that would satisfy the customer order, and

(b) provides the customer with a meaningful opportunity to opt in to the Rule 5320 protections with respect to all or any portion of its order.

If the customer does not opt in to the Rule 5320 protections with respect to all or any portion of its order, the member may reasonably conclude that such customer has consented to the member trading a security on the same side of the market for its own account at a price that would satisfy the customer's order.

In lieu of providing written disclosure to customers at account opening and annually thereafter, a member may provide clear and comprehensive oral disclosure to and obtain consent from the customer on an order-by-order basis, provided that the member documents who provided such consent and such consent evidences the customer's understanding of the terms and conditions of the order.

.02 No-Knowledge Exception

(a) With respect to NMS stocks, as defined in Rule 600 of SEC Regulation NMS, if a member implements and utilizes an effective system of internal controls, such as appropriate information barriers, that operate to prevent one trading unit from obtaining knowledge of customer orders held by a separate trading unit, those other trading units

trading in a proprietary capacity may continue to trade at prices that would satisfy the customer orders held by the separate trading unit. A member that structures its order handling practices in NMS stocks to permit its market-making desk to trade at prices that would satisfy customer orders held by a separate trading unit must disclose in writing to its customers, at account opening and annually thereafter, a description of the manner in which customer orders are handled by the member and the circumstances under which the member may trade proprietarily at its market-making desk at prices that would satisfy the customer order.

(b) With respect to OTC equity securities, as defined in Rule 6420, if a member implements and utilizes an effective system of internal controls, such as appropriate information barriers, that operate to prevent a non-market-making trading unit from obtaining knowledge of customer orders held by a separate trading unit, the non-market-making trading unit trading in a proprietary capacity may continue to trade at prices that would satisfy the customer orders held by the separate trading unit.

.03 Riskless Principal Exception. The obligations under this Rule shall not apply to a member's proprietary trade if such proprietary trade is for the purposes of facilitating the execution, on a riskless principal basis, of an order from a customer (whether its own customer or the customer of another broker-dealer) (the "facilitated order"), provided that the member:

(a) submits a report, contemporaneously with the execution of the facilitated order, identifying the trade as riskless principal to FINRA (or another self-regulatory organization if not required under FINRA rules); and

(b) has written policies and procedures to ensure that riskless principal transactions for which the member is relying upon this exception comply with applicable FINRA rules. At a minimum these policies and procedures must require that the customer order was received prior to the offsetting principal transaction, and that the offsetting principal transaction is at the same price as the customer order exclusive of any markup or markdown, commission equivalent or other fee and is allocated to a riskless principal or customer account in a consistent manner and within 60 seconds of execution.

Members must have supervisory systems in place that produce records that enable the member and FINRA to reconstruct accurately, readily, and in a time-sequenced manner all facilitated orders for which the member relies on this exception.

.04 ISO Exception. A member shall be exempt from the obligation to execute a customer order in a manner consistent with this Rule with regard to trading for its own account that is the result of an intermarket sweep order routed in compliance with Rule 600(b)(30)(ii) of SEC Regulation NMS (“ISO”) where the customer order is received after the member routed the ISO. Where a member routes an ISO to facilitate a customer order and that customer has consented to not receiving the better prices obtained by the ISO, the member also shall be exempt with respect to any trading for its own account that is the result of the ISO with respect to the consenting customer’s order.

.05 Odd Lot and Bona Fide Error Transaction Exceptions. The obligations under this Rule shall not apply to a member’s proprietary trade that is (1) to offset a customer order that is in an amount less than a normal unit of trading; or (2) to correct a bona fide error. Members are required to demonstrate and document the basis upon which a transaction meets the bona fide error exception.

.06 Minimum Price Improvement Standards. The minimum amount of price improvement necessary for a member to execute an order on a proprietary basis when holding an unexecuted limit order in that same security, and not be required to execute the held limit order is as follows:

(a) For customer limit orders priced greater than or equal to \$1.00, the minimum amount of price improvement required is \$0.01 for NMS stocks and the lesser of \$0.01 or one-half (1/2) of the current inside spread for OTC equity securities;

(b) For customer limit orders priced greater than or equal to \$0.01 and less than \$1.00, the minimum amount of price improvement required is the lesser of \$0.01 or one-half (1/2) of the current inside spread;

(c) For customer limit orders priced less than \$0.01 but greater than or equal to \$0.001, the minimum amount of price improvement required is the lesser of \$0.001 or one-half (1/2) of the current inside spread;

(d) For customer limit orders priced less than \$0.001 but greater than or equal to \$0.0001, the minimum amount of price improvement required is the lesser of \$0.0001 or one-half (1/2) of the current inside spread;

(e) For customer limit orders priced less than \$0.0001 but greater than or equal to \$0.00001, the minimum amount of price improvement required is the lesser of \$0.00001 or one-half (1/2) of the current inside spread;

(f) For customer limit orders priced less than \$0.00001, the minimum amount of price improvement required is the lesser of \$0.000001 or one-half (1/2) of the current inside spread; and

(g) For customer limit orders priced outside the best inside market, the minimum amount of price improvement required must either meet the requirements set forth above or the member must trade at a price at or inside the best inside market for the security.

For purposes of determining the minimum price improvement standards for customer limit orders in OTC equity securities priced below \$1.00 where there is no published current inside spread, members may calculate a current inside spread by contacting and obtaining priced quotations from at least two unaffiliated dealers and using the highest bid and lowest offer obtained in calculating the current inside spread. Where there is only a one-sided quote in an OTC equity security priced below \$1.00, members may calculate the current inside spread by contacting and obtaining priced quotations from at least two unaffiliated dealers and using the best price obtained on the other side of the quote. Members must document the name of each dealer contacted and the quotations received for purposes of determining the current inside spread.

In addition, if the minimum price improvement standards above would trigger the protection of a pending customer limit order, any better-priced customer limit order(s) must also be protected under this Rule, even if those better-priced limit orders would not be directly triggered under the minimum price improvement standards above.

.07 Order Handling Procedures. A member must make every effort to execute a marketable customer order that it receives fully and promptly. A member that is holding a customer order that is marketable and has not been immediately executed must make every effort to cross such order with any other order received by the member on the other side of the market up to the size of such order at a price that is no less than the best bid and no greater than the best offer at the time that the subsequent order is received by the

member and that is consistent with the terms of the orders. In the event that a member is holding multiple orders on both sides of the market that have not been executed, the member must make every effort to cross or otherwise execute such orders in a manner that is reasonable and consistent with the objectives of this Rule and with the terms of the orders. A member can satisfy the crossing requirement by contemporaneously buying from the seller and selling to the buyer at the same price.

.08 Trading Outside Normal Market Hours. Members generally may limit the life of a customer order to the period of normal market hours of 9:30 a.m. to 4:00 p.m. Eastern Time. However, if the customer and member agree to the processing of the customer's order outside normal market hours, the protections of this Rule shall apply to that customer's order(s) at all times the customer order is executable by the member.

* * * * *

**Text of NASD Rules and Interpretive Material
to be Deleted in their
Entirety from the Transitional Rulebook**

NASD Rules

* * * * *

[IM-2110-2. Trading Ahead of Customer Limit Order]

Entire text deleted.

* * * * *

[2111. Trading Ahead of Customer Market Orders]

Entire text deleted.

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