

## §41.27

## 17 CFR Ch. I (4–1–10 Edition)

derivatives transaction execution facility may raise or lower the position limit for that security future effective no earlier than the day after it has provided notification to the Commission and to the public under the submission requirements of §41.24. If the data require imposition of a reduced position limit for a security future, the designated contract market or registered derivatives transaction execution facility may permit any trader holding a position in compliance with the previous position limit, but in excess of the reduced limit, to maintain such position through the expiration of the security futures contract; provided that the designated contract market or registered derivatives transaction execution facility does not find that the position poses a threat to the orderly expiration of such contract.

(b) *Final settlement prices for security futures products.* (1) The final settlement price of a cash-settled security futures product must fairly reflect the opening price of the underlying security or securities;

(2) Notwithstanding paragraph (b)(1) of this section, if an opening price for one or more securities underlying a security futures product is not readily available, the final settlement price of the security futures product shall fairly reflect:

(i) The price of the underlying security or securities during the most recent regular trading session for such security or securities; or

(ii) The next available opening price of the underlying security or securities.

(3) Notwithstanding paragraphs (b)(1) or (b)(2) of this section, if a derivatives clearing organization registered under Section 5b of the Act or a clearing agency exempt from registration pursuant to Section 5b(a)(2) of the Act, to which the final settlement price of a security futures product is or would be reported determines, pursuant to its rules, that such final settlement price is not consistent with the protection of customers and the public interest, taking into account such factors as fairness to buyers and sellers of the affected security futures product, the maintenance of a fair and orderly market in such security futures product,

and consistency of interpretation and practice, the clearing organization shall have the authority to determine, under its rules, a final settlement price for such security futures product.

(c) *Special requirements for physical delivery contracts.* For security futures products settled by actual delivery of the underlying security or securities, payment and delivery of the underlying security or securities must be effected through a clearing agency that is registered pursuant to section 17A of the Securities Exchange Act of 1934.

(d) The Commission may exempt from the provisions of paragraphs (a)(2) and (b) of this section, either unconditionally or on specified terms and conditions, any designated contract market or registered derivatives transaction execution facility, if the Commission determines that such exemption is consistent with the public interest and the protection of customers. An exemption granted pursuant to this paragraph shall not operate as an exemption from any Securities and Exchange Commission rules. Any exemption that may be required from such rules must be obtained separately from the Securities and Exchange Commission.

[66 FR 55083, Nov. 1, 2001, as amended at 67 FR 36761, May 24, 2002]

### **§41.27 Prohibition of dual trading in security futures products by floor brokers.**

(a) *Definitions.* For purposes of this section:

(1) Trading session means hours during which a designated contract market or registered derivatives transaction execution facility is scheduled to trade continuously during a trading day, as set forth in its rules, including any related post settlement trading session. A designated contract market or registered derivatives transaction execution facility may have more than one trading session during a trading day.

(2) Member shall have the meaning set forth in section 1a(24) of the Act.

(3) Broker association includes two or more designated contract market or registered derivatives transaction execution facility members with floor

trading privileges of whom at least one is acting as a floor broker who:

- (i) Engage in floor brokerage activity on behalf of the same employer;
- (ii) Have an employer and employee relationship which relates to floor brokerage activity;
- (iii) Share profits and losses associated with their brokerage or trading activity; or
- (iv) Regularly share a deck of orders.

(4) Customer means an account owner for which a trade is executed other than:

- (i) An account in which such floor broker has any interest;
- (ii) An account for which a floor broker has discretion;
- (iii) An account controlled by a person with whom a floor broker has a relationship through membership in a broker association;
- (iv) A house account of the floor broker's clearing member; or
- (v) An account for another member present on the floor of a designated contract market or registered derivatives transaction execution facility or an account controlled by such other member.

(5) Dual trading means the execution of customer orders by a floor broker through open outcry during the same trading session in which the floor broker executes directly or by initiating and passing to another member, either through open outcry or through a trading system that electronically matches bids and offers pursuant to a predetermined algorithm, a transaction for the same security futures product on the same designated contract market or registered derivatives transaction execution facility for an account described in paragraphs (a)(4)(i)-(v) of this section.

(b) *Dual Trading Prohibition.* (1) No floor broker shall engage in dual trading in a security futures product on a designated contract market or registered derivatives transaction execution facility, except as otherwise provided under paragraphs (d), (e), and (f) of this section.

(2) A designated contract market or a registered derivatives transaction execution facility operating an electronic market or electronic trading system that provides market participants with

a time or place advantage or the ability to override a predetermined algorithm must submit an appropriate rule proposal to the Commission consistent with the procedures set forth in §40.5. The proposed rule must prohibit electronic market participants with a time or place advantage or the ability to override a predetermined algorithm from trading a security futures product for accounts in which these same participants have any interest during the same trading session that they also trade the same security futures product for other accounts. This paragraph, however, is not applicable with respect to execution priorities or quantity guarantees granted to market makers who perform that function, or to market participants who receive execution priorities based on price improvement activity, in accordance with the rules governing the designated contract market or registered derivatives transaction execution facility.

(c) *Rules Prohibiting Dual Trading—(1) Designated contract markets.* Prior to listing a security futures product for trading on a trading floor where bids and offers are executed through open outcry, a designated contract market:

(i) Must submit to the Commission in accordance with §40.6, a rule prohibiting dual trading, together with a written certification that the rule complies with the Act and the regulations thereunder, including this section; or

(ii) Must obtain Commission approval of such rule pursuant to §40.5.

(2) *Registered derivatives transaction execution facilities.* Prior to listing a security futures product for trading on a trading floor where bids and offers are executed through open outcry, a registered derivatives transaction execution facility:

(i) Must notify the Commission in accordance with §37.7(b) that it has adopted a rule prohibiting dual trading; or

(ii) Must obtain Commission approval of such rule pursuant to §37.7(c).

(d) *Specific Permitted Exceptions.* Notwithstanding the applicability of a dual trading prohibition under paragraph (b) of this section, dual trading may be permitted on a designated contract market or a registered derivatives transaction execution facility

pursuant to one or more of the following specific exceptions:

(1) *Correction of errors.* To offset trading errors resulting from the execution of customer orders, provided, that the floor broker must liquidate the position in his or her personal error account resulting from that error through open outcry or through a trading system that electronically matches bids and offers as soon as practicable, but, except as provided herein, not later than the close of business on the business day following the discovery of error. In the event that a floor broker is unable to offset the error trade because the daily price fluctuation limit is reached, a trading halt is imposed by the designated contract market or registered derivatives transaction execution facility, or an emergency is declared pursuant to the rules of the designated contract market or registered derivatives transaction execution facility, the floor broker must liquidate the position in his or her personal error account resulting from that error as soon as practicable thereafter.

(2) *Customer consent.* To permit a customer to designate in writing not less than once annually a specifically identified floor broker to dual trade while executing orders for such customer's account. An account controller acting pursuant to a power of attorney may designate a dual trading broker on behalf of its customer, provided, that the customer explicitly grants in writing to the individual account controller the authority to select a dual trading broker.

(3) *Spread transactions.* To permit a broker who unsuccessfully attempts to leg into a spread transaction for a customer to take the executed leg into his or her personal account and to offset such position, provided, that a record is prepared and maintained to demonstrate that the customer order was for a spread.

(4) *Market emergencies.* To address emergency market conditions resulting in a temporary emergency action as determined by a designated contract market or registered derivatives transaction execution facility.

(e) *Rules Permitting Specific Exceptions—(1) Designated contract markets.* Prior to permitting dual trading under

any of the exceptions provided in paragraphs (d)(1)–(4) of this section, a designated contract market:

(i) Must submit to the Commission in accordance with § 40.6, a rule permitting the exception(s), together with a written certification that the rule complies with the Act and the regulations thereunder, including this section; or

(ii) Must obtain Commission approval of such rule pursuant to § 40.5.

(2) *Registered derivatives transaction execution facilities.* Prior to permitting dual trading under any of the exceptions provided in paragraphs (d)(1)–(4) of this section, a registered derivatives transaction execution facility:

(i) Must notify the Commission in accordance with § 37.7(b) that it has adopted a rule permitting the exception(s); or

(ii) Must obtain Commission approval of such rule pursuant to § 37.7(c).

(f) *Unique or Special Characteristics of Agreements, Contracts, or Transactions, or of Designated Contract Markets or Registered Derivatives Transaction Execution Facilities.* Notwithstanding the applicability of a dual trading prohibition under paragraph (b) of this section, dual trading may be permitted on a designated contract market or registered derivatives transaction execution facility to address unique or special characteristics of agreements, contracts, or transactions, or of the designated contract market or registered derivatives transaction execution facility as provided herein. Any rule of a designated contract market or registered derivatives transaction execution facility that would permit dual trading when it would otherwise be prohibited, based on a unique or special characteristic of agreements, contracts, or transactions, or of the designated contract market or registered derivatives transaction execution facility must be submitted to the Commission for prior approval under the procedures set forth in § 40.5. The rule submission must include a detailed demonstration of why an exception is warranted.

[67 FR 11227, Mar. 13, 2002]