

with such member's usual practice or as required by any State or Federal securities laws, or any rule or regulation thereunder.

FINRA proposed amending the requirements of NASD Rule 2270 to provide an alternative means of satisfying the requirement that members make balance sheet information available to bona fide regular customers. Currently, the rule requires that members "make available to inspection by any bona fide regular customer, upon request, the information relative to such member's financial condition as disclosed in its most recent balance sheet \* \* \*." FINRA proposed providing members with the option of delivering their balance sheet, in paper or electronic form, to customers who request it. With respect to electronic delivery, the requesting customer must consent to receive the balance sheet in electronic form to ensure that such information is accessible to the customer. FINRA did not propose requiring members to deliver their balance sheet to all customers (instead of making them available to inspection or delivering them upon request) because Rule 17a-5(c) under the Act<sup>6</sup> generally requires a broker-dealer that carries customer accounts to send its full balance sheet and certain other financial information to each of its customers twice a year.<sup>7</sup> NASD Rule 2270 provides customers with additional access to their broker's balance sheet information by requiring that members permit customers to inspect or obtain a copy of a member's most recent balance sheet at any time upon request.

NASD Rule 2910 requires any member that is a party to an open transaction or who has on deposit cash or securities of another member to furnish, upon the written request of the other member, a statement of its financial condition as disclosed in its most recently prepared balance sheet. FINRA proposed amending the provisions of NASD Rule 2910 to require, consistent with NASD Rule 2270, that members provide to other members the balance sheet that was "prepared either in accordance with

such member's usual practice or as required by any State or Federal securities laws, or any rule or regulation thereunder." In addition, FINRA proposed that members be permitted to provide their balance sheet to other members in paper or electronic form. However, unlike the proposed amendments to NASD Rule 2270, FINRA did not propose requiring members to obtain the consent of other members to electronically deliver the balance sheet. FINRA believes that other members, unlike all customers, will be equipped to receive electronic delivery.

FINRA believes that the requirements of NASD Rule 2270 and NASD Rule 2910 continue to provide access to important information by allowing customers and other members to have access to a copy of a member's most recent balance sheet at any time upon request and should be transferred, as amended, to the Consolidated FINRA Rulebook as FINRA Rule 2261.

FINRA will announce the implementation date of the proposed rule change in a *Regulatory Notice* to be published no later than 90 days following Commission approval.

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.<sup>8</sup> In particular, the Commission finds that the proposal is consistent with Section 15A(b)(6) of the Act,<sup>9</sup> which requires, among other things, that FINRA's rules 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 rule change will further the purposes of the Act by, among other things, ensuring that basic, current information regarding the financial condition of members with which customers and other members conduct business is available upon request. The Commission therefore believes that it is appropriate and consistent with the Act for FINRA to Adopt FINRA Rule 2261 (Disclosure of Financial Condition) in the Consolidated FINRA Rulebook.

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Act,<sup>10</sup> that the proposed rule change (SR-FINRA-2009-081) is approved.

<sup>8</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>9</sup> 15 U.S.C. 78o-3(b)(6).

<sup>10</sup> 15 U.S.C. 78s(b)(2).

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>11</sup>

**Florence E. Harmon,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-61537; File No. SR-FINRA-2009-095]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change To Adopt FINRA Rule 3240 (Borrowing From or Lending to Customers) in the Consolidated FINRA Rulebook

February 18, 2010.

#### I. Introduction

On December 31, 2009, Financial Industry Regulatory Authority, Inc. ("FINRA") (f/k/a National Association of Securities Dealers, Inc. ("NASD")) filed with the Securities and Exchange Commission ("SEC" or "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to adopt NASD Rule 2370 (Borrowing From or Lending to Customers) as FINRA Rule 3240 (Borrowing From or Lending to Customers) in the Consolidated FINRA Rulebook<sup>3</sup> with certain changes and to delete Incorporated NYSE Rules 352(e) (Limitations on Borrowing From or Lending to Customers), (f) (Loan Procedures) and (g). The proposed rule change would also add a Supplementary Material section regarding record retention requirements to proposed FINRA Rule 3240. The proposed rule change was published for comment in the **Federal Register** on January 12, 2010.<sup>4</sup> The Commission received no

<sup>11</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 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 members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE ("Dual Members"). The FINRA Rules apply to all FINRA members, unless such rules have a more limited application by their terms. For more information about the rulebook consolidation process, see *Information Notice*, March 12, 2008 (Rulebook Consolidation Process).

<sup>4</sup> See Securities Exchange Act Release No. 61302 (January 6, 2010), 75 FR 1672 (January 12, 2010).

<sup>6</sup> 17 CFR 240.17a-5(c).

<sup>7</sup> SEC Rule 17a-5(c)(5) contains a conditional exemption from the requirement that broker-dealers semi-annually send customers a full balance sheet. Under the exemption, a broker-dealer can semi-annually send its customers summary information regarding its net capital, as long as it also provides customers with a toll-free number to call for a free copy of its full balance sheet, makes its full balance sheet available to customers on its Web site, and meets other specified requirements. See Securities Exchange Act Release No. 48272 (August 1, 2003), 68 FR 46446 (August 6, 2003).

comments on the proposed rule change. This order approves the proposed rule change.

## II. Description of the Proposed Rule Change

FINRA proposed adopting NASD Rule 2370 as FINRA Rule 3240 in the Consolidated FINRA Rulebook with certain changes as described below. FINRA also proposed deleting Incorporated NYSE Rules 352(e) through (g)<sup>5</sup> from the Transitional Rulebook.<sup>6</sup> Further, the proposed rule change would also add a Supplementary Material section regarding record retention requirements to proposed FINRA Rule 3240.

### A. Background

The purpose of NASD Rule 2370 is to give FINRA member broker-dealers the opportunity to evaluate the appropriateness of particular lending arrangements between their registered persons and customers, to the extent permitted by the member, and the potential for conflicts of interests between both the registered person and his or her customer and the registered person and the member with which he or she is associated.

To that end, NASD Rule 2370 prohibits registered persons from borrowing money from or lending money to their customers (collectively referred to as "lending arrangements") unless certain conditions are met. Specifically, under Rule 2370, no registered person may borrow money from or lend money to his or her customer unless the firm has written procedures allowing such lending arrangements and (1) the customer is a member of the registered person's immediate family;<sup>7</sup> (2) the customer is in the business of lending money; (3) the customer and the registered person are both registered persons of the same firm; (4) the lending arrangement is based on a personal relationship outside of the broker-customer relationship; or (5) the lending arrangement is based on a business relationship outside of the broker-customer relationship. In addition, with the exception of lending

arrangements between immediate family members and lending arrangements between registered persons and customers in the business of lending money, FINRA members are required to pre-approve in writing the other lending arrangements described above.

With respect to lending arrangements between immediate family members, a FINRA member's written procedures may indicate that the member permits such lending arrangements and that registered persons need not notify the member or receive member approval for such lending arrangements.

For lending arrangements between registered persons and customers in the business of lending money, a member's written procedures may indicate that registered persons are not required to notify the member or receive member approval for such lending arrangements, provided that such lending arrangements have been made on commercial terms that the customer generally makes available to members of the general public who are similarly situated as to need, purpose and creditworthiness.<sup>8</sup> Further, the member need not investigate such lending arrangements, but may rely on the registered person's representation that the terms of the loan meet these standards.

It is important to note that members can choose to permit registered persons to borrow money from or lend money to their customers consistent with the requirements of the rule or prohibit the practice in whole or in part.

NYSE Rules 352(e) through (g) also govern lending arrangements between registered persons and their customers. These provisions are substantially similar to the provisions of NASD Rule 2370, with one exception. NYSE Rule 352(f) provides an exception from the pre-approval requirements of the rule for loans totaling \$100 or less between registered persons of the same firm.

### B. Proposal

FINRA proposed adopting NASD Rule 2370 as FINRA Rule 3240 in the Consolidated FINRA Rulebook, subject to the following changes. FINRA proposed amending paragraph (a) (Permissible Lending Arrangements; Conditions) of the rule to indicate more explicitly that such arrangements are subject to the procedural requirements set forth in paragraph (b) (Notification and Approval) of the rule. FINRA also

proposed amending paragraph (a)(2)(B) of the rule regarding permissible lending arrangements between registered persons and customers in the business of lending money to indicate more explicitly that such customers must be acting in the course of such business.

Further, FINRA proposed amending paragraph (b)(1) of the rule to require expressly that registered persons notify their member firms of the lending arrangements that require member pre-approval (FINRA proposed this change for purposes of consistency with paragraphs (b)(2) and (3) of the rule, which provide that a registered person is not required either to notify the member or receive member approval for certain specified lending arrangements) and to clarify that any modifications to such lending arrangements (including any extension of the duration of such arrangements) are also subject to notification and member pre-approval.

In addition, FINRA proposed amending the definition of "immediate family" in paragraph (c) (Definition of Immediate Family) of the rule to replace the reference that the term "includes" the enumerated persons to reflect that the term "means" such persons. Finally, FINRA proposed adding Supplementary Material .01 (Record Retention) requiring that members preserve the written pre-approval required by the rule for at least three years after the date that the lending arrangement has terminated or for at least three years after the registered person's association with the member has terminated. FINRA proposed deleting NYSE Rules 352(e) through (g) as the provisions of the NYSE rules are substantially similar to NASD Rule 2370.

FINRA will announce the implementation date of the proposed rule change in a *Regulatory Notice* to be published no later than 90 days following Commission approval. The implementation date will be no later than 180 days following Commission approval.

## III. Discussion and Findings

After a careful review of the proposal, the Commission finds that the proposed rule change is consistent with the requirements of the Exchange Act and the rules and regulations thereunder applicable to FINRA.<sup>9</sup> In particular, the Commission finds that the proposed rule change is consistent with Section

<sup>5</sup> For convenience, the Incorporated NYSE Rules are referred to as the NYSE Rules.

<sup>6</sup> NYSE Rules 352(a) through (d) were deleted as part of a prior rule change. See Securities Exchange Act Release No. 60701 (September 21, 2009), 74 FR 49425 (September 28, 2009) (Order Approving File No. SR-FINRA-2009-014).

<sup>7</sup> NASD Rule 2370 defines the term "immediate family" to include parents, grandparents, mother-in-law or father-in-law, husband or wife, brother or sister, brother-in-law or sister-in-law, son-in-law or daughter-in-law, children, grandchildren, cousin, aunt or uncle, or niece or nephew, and any other person whom the registered person supports, directly or indirectly, to a material extent.

<sup>8</sup> The fact that a registered person can negotiate a better rate or terms for a loan that is not the product of the broker-customer relationship would not vitiate the idea that the loan occurred on terms generally offered to the public. See *Notice to Members* 04-14 (March 2004).

<sup>9</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

15A(b)(6) of the Exchange Act,<sup>10</sup> which requires, among other things, that FINRA's rules be designed to prevent fraud and manipulative practices and to promote just and equitable principles of trade and, in general, to protect investors and the public interest. The Commission believes that the proposed rule change is reasonably designed to achieve these ends by providing FINRA member broker-dealers the opportunity to evaluate the appropriateness of certain lending arrangements between their registered persons and others, to the extent permitted by a FINRA member broker-dealer, and the potential that these lending arrangements could create certain conflicts of interest.

#### IV. Conclusion

*It is therefore ordered*, pursuant to Section 19(b)(2) of the Exchange Act,<sup>11</sup> that the proposed rule change (SR-FINRA-2009-095) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>12</sup>

**Florence E. Harmon,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-61535; File No. SR-NYSEAmex-2010-14]

### Self-Regulatory Organizations; NYSE Amex LLC; Notice of Filing of Proposed Rule Change Amending Position Limits for Certain Exchange Traded Funds

February 18, 2010.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act" or "Exchange Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 17, 2010, NYSE Amex LLC ("NYSE Amex" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to (a) amend the Position Limits for certain highly liquid Exchange Traded Funds ("ETFs"); (b) memorialize a previously approved provision that was never inserted in the Exchange's Rules, as well as clarify its applicable scope, and (c) amend certain rules to define certain contract terms. The text of the proposed rule change is available on NYSE Amex's Web site at (<http://www.nyse.com>), on the Commission's Web site at <http://www.sec.gov>, at NYSE Amex, and at the Commission's Public Reference Room.

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

##### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

The purpose of this filing is to (a) eliminate Position Limits in certain highly active ETFs, (b) memorialize a previously approved provision that was never inserted in the Exchange's Rules, as well as clarify its applicable scope, and (c) amend certain rules to define certain contract terms. The provision at issue—allowing for option contracts on ETFs that overly 1,000 shares ("Jumbo options")—was approved in 1998, but did not include changes to Rule Text at that time.<sup>3</sup> In order to resume listing these products, the Exchange is proposing to restrict the listing of Jumbo options to four specific ETFs that have no Position Limit (as proposed below), and also define how strike prices and premiums will be expressed for Jumbo contracts by amending Rule 903 and Rule 959NY.<sup>4</sup>

<sup>3</sup> Exchange Act Release No. 40157, File No. SR-Amex-96-44 (July 1, 1998) 63 FR 37426 (July 10, 1998).

<sup>4</sup> SR-Amex-96-44 was also silent on the manner of expressing strike prices and premium bids and offers, thus it is necessary to define them in this filing.

#### Position Limits

Four ETFs have been approved under NYSE Amex Rule 904 to have exceptional Position Limits. These are NASDAQ 100 Tracking Stock (QQQQ); SPDR S&P 500 ETF (SPY); iShares Russell 2000 Index Fund (IWM); and DIAMONDS Trust (DIA). NYSE Amex proposes that these four ETFs have no Position Limit.

Position and Exercise limits were introduced as a means of forestalling the potential manipulation of an equity's price by someone that established a large option position. This concern was mitigated with cash settled index options since the contract settled for cash as opposed to physical shares of stock. Additionally, those index options whose position limits have been eliminated are based on a broad based index comprised of many equities further mitigating concerns about manipulation through the establishment and subsequent exercise of a large options position. This resulted in a repeal of position and exercise limits for the options on the aforementioned broad based indexes.<sup>5</sup>

While ETF options are physically settled, NYSE Amex feels that there are specific aspects related to an ETF's structure that serve to mitigate any concerns about manipulation and allow eliminating position limits on a narrow subset of the ETF option universe. First, ETFs are structured as open-ended trusts or mutual funds that can continually issue new shares as required to satisfy demand. This is in sharp contrast to an equity that has a float that is only increased by corporate action and is not a function of investor demand. Second, the ETF itself is comprised of a basket of stocks, specifically those that comprise a benchmark broad based index.

Additionally, in approving the elimination of position and exercise limits for RUT, NDX, DJX, and SPX options, the Commission considered the capitalization of the components of each of these indexes and the deep and liquid markets for the securities underlying each index significantly reduced concerns of market manipulation or disruption in the underlying markets.

Shares in these four underlying ETFs have exceptionally high trading volume, demonstrating extraordinary liquidity. The volume for each of these ETFs for

<sup>5</sup> See Securities Exchange Act Release No. 56351 (September 4, 2007); see also Securities Exchange Act Release No. 52649 (October 21, 2005), 70 FR 62146 (October 28, 2005) (SR-Amex-2005-063) ("NDX Approval Order"); see also Securities Exchange Act Release No. 46393 (August 21, 2002), 67 FR 55289 (August 28, 2002) (SR-Amex-2002-31) ("XMI/XII Permanent Approval Order").

<sup>10</sup> 15 U.S.C. 78o-3(b)(6).

<sup>11</sup> 15 U.S.C. 78s(b)(2).

<sup>12</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.