

available publicly. All submissions should refer to File Number SR-CBOE-2010-043 and should be submitted on or before June 25, 2010.

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. 34-62199; File No. SR-FINRA-2010-026]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change To Adopt FINRA Rule 5121 (Public Offerings of Securities With Conflicts of Interest) in the Consolidated FINRA Rulebook

June 1, 2010.

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> notice is hereby given that on May 20, 2010, 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”) the proposed rule change as described in Items I, II, and III below, which Items have been substantially prepared by FINRA. 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

FINRA is proposing to adopt NASD Rule 2720 (Public Offerings of Securities With Conflicts of Interest) as a FINRA rule in the consolidated FINRA rulebook without material change. The proposed rule change would renumber NASD Rule 2720 as FINRA Rule 5121 in the consolidated FINRA rulebook.

The text of the proposed rule change is available on FINRA’s Web site at <http://www.finra.org>, at the principal office of FINRA 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, FINRA 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 these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

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

###### 1. Purpose

As part of the process of developing a new consolidated rulebook (“Consolidated FINRA Rulebook”),<sup>3</sup> FINRA is proposing to adopt NASD Rule 2720 (Public Offerings of Securities With Conflicts of Interest) without material change as FINRA Rule 5121 in the Consolidated FINRA Rulebook.

NASD Rule 2720 governs public offerings of securities in which a member with a conflict of interest participates. The rule generally prohibits a member with a “conflict of interest,” as defined in the rule,<sup>4</sup> from participating in a public offering, unless

<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> As defined in NASD Rule 2720(f)(5), a conflict of interest exists, if at the time of a member’s participation in an entity’s public offering, any of the following four conditions applies: (1) The securities are to be issued by the member; (2) the issuer controls, is controlled by or is under common control with the member or the member’s associated persons; (3) at least five percent of the net offering proceeds, not including underwriting compensation, are intended to be (i) used to reduce or retire the balance of a loan or credit facility extended by the member, its affiliates and its associated persons, in the aggregate; or (ii) otherwise directed to the member, its affiliates and associated persons, in the aggregate; or (4) if, as a result of the public offering and any transactions contemplated at the time of the public offering (i) the member will be an affiliate of the issuer; (ii) the member will become publicly owned; or (iii) the issuer will become a member or form a broker-dealer subsidiary. NASD Rule 2720 defines several terms for purposes of the rule, including “entity,” “control,” and “common control.”

certain other requirements are met.<sup>5</sup> There is no comparable Incorporated NYSE Rule.

On June 15, 2009, the SEC approved a proposed rule change to modernize NASD Rule 2720 (the “2009 Rule Change”).<sup>6</sup> The 2009 Rule Change became effective on September 14, 2009.<sup>7</sup>

The proposed rule change would adopt NASD Rule 2720 without material change as FINRA Rule 5121 in the Consolidated FINRA Rulebook. The rule would make minor changes to reflect the new terminology conventions of the Consolidated FINRA Rulebook.

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 from Commission approval.

###### 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>8</sup> which requires, among other things, that FINRA rules must 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. FINRA believes that the proposed rule change will continue to serve to protect investors in offerings where the member has a conflict of interest.

##### B. Self-Regulatory Organization’s Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

##### C. Self-Regulatory Organization’s Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

Written comments were neither solicited nor received.

<sup>5</sup> The rule requires prominent disclosure of the nature of the conflict, and in certain circumstances, the participation of a qualified independent underwriter. Members also must comply with certain net capital, discretionary accounts and filing requirements, as applicable.

<sup>6</sup> See Securities Exchange Act Release No. 60113 (June 15, 2009), 74 FR 29255 (June 19, 2009) (Order Approving Proposed Rule Change; File No. SR-FINRA-2007-009).

<sup>7</sup> See *Regulatory Notice* 09-49 (SEC Approves Amendments to Modernize and Simplify NASD Rule 2720 Relating to Public Offerings in Which a Member Firm With a Conflict of Interest Participates) (August 2009).

<sup>8</sup> 15 U.S.C. 78o-3(b)(6).

<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.

### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 35 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

- (A) By order approve such proposed rule change, or
- (B) Institute proceedings to determine whether the proposed rule change should be disapproved.

### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

#### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2010-026 on the subject line.

#### *Paper Comments*

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549-1090.

All submissions should refer to File Number SR-FINRA-2010-026. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official

business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2010-026 and should be submitted on or before June 25, 2010.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>9</sup>

**Florence E. Harmon,**  
*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-62190; File No. SR-CBOE-2010-021]

### Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Order Approving Proposed Rule Change as Modified by Amendment No. 1 Thereto Relating to Correlated Instrument Delta Hedge Exemption

May 27, 2010.

On March 19, 2010, the Chicago Board Options Exchange, Incorporated ("Exchange" or "CBOE") filed with the Securities and Exchange Commission ("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 (i) expand the delta hedging exemption available for equity options position limits; (ii) amend the reporting requirements applicable to members relying on the delta hedging exemption; and (iii) adopt a delta hedging exemption from certain index options position limits. The proposed rule change was published for comment in the **Federal Register** on April 2, 2010.<sup>3</sup> On May 19, 2010, CBOE filed Amendment No. 1 to the proposal.<sup>4</sup> The Commission received no comment

<sup>9</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> See Securities Exchange Act Release No. 61785 (March 25, 2010), 75 FR 16888.

<sup>4</sup> Amendment No. 1 deleted the word "or" from the rule text of the proposal and deleted a footnote from the purpose section and Exhibit 1 of the proposal. Because the amendment does not affect the substance of the rule filing, the amendment does not require notice and comment.

letters on the proposal. This order approves the proposed rule change, as modified by Amendment No. 1.

In December 2007, the Commission approved a CBOE proposal to create an exemption from position and exercise limits applicable to equity options (stock options and options on exchange-traded funds) for positions held by CBOE members and certain non-member affiliates that are delta neutral<sup>5</sup> under a "permitted pricing model"<sup>6</sup> ("Equity Exemption").<sup>7</sup> When a position is not delta neutral, only the option contract equivalent of the net delta<sup>8</sup> of the position remains subject to the position limits in Rule 4.11. Currently, the Equity Exemption is available only for securities that directly underlie the applicable option position. For example, with respect to options on exchange-traded funds ("ETF options"), index options overlying the same index on which the ETF is based currently cannot be combined with the ETF options to calculate a net delta for purposes of the Equity Exemption.

The proposed rule change would expand the Equity Exemption by permitting equity option positions for which the underlying security is an ETF that is based on the same index as an index option to be combined with any position in the underlying ETF as well as any position in an index option and/or a correlated instrument for calculation of the Equity Exemption.<sup>9</sup> The term "correlated instrument" would

<sup>5</sup> "Delta neutral" is defined as a precise term for purposes of the Equity Exemption in Rule 4.11.04(c)(A).

<sup>6</sup> Under Rule 4.11.04(c)(C), "permitted pricing model" for purposes of the Equity Exemption is a pricing model: (1) Maintained and operated by the Options Clearing Corporation ("OCC Model"); (2) maintained and used by a member or its non-member affiliate subject to consolidated supervision by the Commission pursuant to Appendix E of Rule 15c3-1, 17 CFR 240.15c3-1, under the Act; (3) maintained and used by a financial holding company ("FHC") or a company treated as an FHC under the Bank Holding Company Act of 1956, or its affiliate subject to consolidated holding company group supervision; (4) maintained and used by a Commission-registered OTC derivatives dealer; or (5) used by a national bank under the National Bank Act.

<sup>7</sup> See Securities Exchange Act Release No. 56970 (December 14, 2007), 72 FR 72428 (December 20, 2007) (SR-CBOE-2007-99) ("Exemption Approval Order"). In August 2009, the Commission approved a CBOE proposal to extend the Equity Exemption to customers. See Securities Exchange Act Release No. 60555 (August 21, 2009), 74 FR 43741 (August 27, 2009) (SR-CBOE-2009-39). The Commission notes that the Equity Exemption is not currently available to customers. See Securities Exchange Act Release No. 61857 (April 7, 2010), 75 FR 18931 (April 13, 2010) (SR-CBOE-2010-30).

<sup>8</sup> "Net delta" is defined as a precise term for the purposes of the Equity Exemption in Rule 4.11.04(c)(B).

<sup>9</sup> However, this would not include baskets of securities for purposes of the delta hedging exemptions.