



Securities Industry Continuing Education Program Firm Element Advisory – Fall 2010

Introduction

The Securities Industry/Regulatory Council on Continuing Education (Council) publishes the Firm Element Advisory (FEA) semi-annually to highlight current regulatory and sales practice topics for possible inclusion in Firm Element training plans. The Council has identified the topics from a review of industry regulatory and self-regulatory organization (SRO) publications and announcements of significant events.

The FEA briefly identifies each topic and provides links to relevant documents issued about the specified subjects. The FEA is designed for Internet use; however, it can be printed. Be advised that each link must be printed separately in order to encompass the full document and subjects covered.

All new material in the FEA is denoted by a “*(New)*” next to the appropriate title. Material from previous editions that the Council has updated is denoted with an “*(Updated)*” next to the appropriate title. The Council removes any material from previously published editions of the FEA that is no longer current.

The Council suggests that firms use the FEA as an aid in developing and updating their Firm Element needs analysis and written training plans. However, firms are reminded that they should not rely on the FEA as a comprehensive list of all areas they should consider. Firms should review the FEA and determine which topics are relevant for inclusion in their training based on their product offerings, structure and business line(s).

In response to requests from firms for more resources to help them with Firm Element planning, the Council suggests the following tools that firms may use in addition to the FEA:

- [**The Firm Element Guidance Document**](#): Suggestions for effectively performing the needs analysis and developing written training plans.
- [**The Firm Element Content Builder**](#): A web-based tool that allows users to search, by keyword, through an extensive database of regulatory resources



related to specific investment products or services (formerly the Firm Element Organizer).

- **Quarterly Continuing Education Performance Reports**: FINRA produces quarterly reports that compare a firm's continuing education performance with the industry at large for the same programs and modules. Firms should review the performance of their registered persons since the last needs analysis to determine if any modules or topics appear to warrant additional training. These reports are no longer mailed, but firms may sign up to view the reports on [FINRA's Report Center](#).
- **FINRA's 2010 Examination Priorities Letter**: Each year, FINRA issues a letter that highlights new and existing areas of significance to FINRA's examination program. These letters may be useful when developing education programs within a firm.
- **FINRA Investor Alerts**: Periodic alerts that highlight products and sales practices of particular concern, which firms may use to supplement training materials.

The Council recommends using all available tools to make Firm Element planning as efficient and effective as possible.

Reminder

Individuals are now required to use either their CRD or FINRA ID numbers to schedule an exam or CE appointment at Prometric or Pearson VUE testing centers. Social Security numbers are no longer accepted.

All non-FINRA candidates who enroll using the Form U10 will be assigned a FINRA ID number for scheduling purposes.

Please note that the Form U10 is now only available for online submission; hardcopy forms mailed to FINRA are no longer accepted.

Questions?

For more information, contact:

- cecounciladmin@finra.org; or
- Roni Meikle, Director, Continuing Education, FINRA, at (646) 315-8688.



ALTERNATIVE INVESTMENTS

Reverse Exchangeable Securities (Reverse Convertibles)

Firms that sell reverse convertibles must ensure that their promotional materials and communications to the public regarding these products are fair and balanced, and do not understate the risks associated with these products. Firms also must ensure that their registered representatives understand the risks, terms and costs associated with these products, and that they perform an adequate suitability analysis before recommending them to any customer.

- [**FINRA Regulatory Notice 10-09**](#): FINRA Reminds Firms of Their Sales Practice Obligations With Reverse Exchangeable Securities (Reverse Convertibles) (February 2010)

Principal-Protected Notes

Firms that sell principal-protected notes must ensure that their promotional materials and communications to the public regarding these products are fair and balanced, and do not overstate either the level of protection offered or an investment's potential returns. Firms also have a duty to ensure that their registered representatives understand the risks, terms and costs associated with these products, and that they perform an adequate suitability analysis before recommending them to any customer.

- [**FINRA Regulatory Notice 09-73**](#): FINRA Reminds Firms of Their Sales Practice Obligations Relating to Principal-Protected Notes (December 2009)

Non-Traditional Exchange-Traded Funds (ETFs)

Leveraged and inverse ETFs are often complex and have unique trading characteristics. For instance, due to the effects of compounding, an ETF's longer-term performance may deviate from its stated daily objective.

Firms that sell leveraged and inverse ETFs must make sure:

- recommendations to customers are suitable and based on a full understanding of the terms and features of the product recommended;



- sales materials related to leveraged and inverse ETFs are fair and accurate; and
 - they have adequate supervisory procedures in place to ensure these obligations are met.
- [FINRA Regulatory Notice 09-31](#): FINRA Reminds Firms of Sales Practice Obligations Relating to Leveraged and Inverse Exchange-Traded Funds (June 2009)

Public Offerings of DPPs and REITs

Firms that provide valuations of Real Estate Investment Trusts (REITs) and Direct Participation Programs (DPPs) on customer account statements must not use par value in a customer account statement more than 18 months following the conclusion of an offering, unless an appraisal of the program's assets and operations yields the same value. Firms also must determine that all material facts are adequately and accurately disclosed, including the amount or composition of the dividend distributions.

- [FINRA Regulatory Notice 09-09](#): Customer Account Statements and Due Diligence Requirements for Unlisted Real Estate Investment Trusts (REITs) and Direct Participation Programs (DPPs) (February 2009)

ANTI-MONEY LAUNDERING

In September 2009, the SEC approved the adoption of NASD Rule 3011 (Anti-Money Laundering (AML) Compliance Program) without substantive change into the Consolidated FINRA Rulebook as FINRA Rule 3310 (AML Compliance Program). The SEC also approved the adoption of NASD IM-3011-1 (Independent Testing Requirements), subject to certain amendments, and NASD IM-3011-2 (Review of AML Compliance Person Information), without substantive change, as supplementary material to FINRA Rule 3310. FINRA Rule 3310 does not retain the exception in NASD IM-3011-1 that permitted, under certain conditions, the AML compliance program testing to be conducted by persons who report to either the AML compliance person or persons performing the functions being tested (the independent testing exception).

The Financial Crimes Enforcement Network (FinCEN), a bureau within the Department of the Treasury that is responsible for administering the Bank Secrecy



Act (BSA) and its implementing regulations, has stated that the independent testing provision of the BSA precludes AML program testing by personnel with an interest in the outcome of the testing, and that an independent testing exception, such as the one in NASD IM-3011-1, is inconsistent with the BSA's independent testing provision and FinCEN's interpretation of this provision. FINRA Rule 3310 took effect on January 1, 2010.

- [FINRA Regulatory Notice 09-60](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules (October 2009)

***(Updated)* AML Compliance**

Firms are reminded to maintain current AML programs and train staff appropriately. Information and guidance relating to AML rules, regulations and compliance is issued regularly from a number of sources, such as the following.

- [FINRA Issue Center: Anti-Money Laundering](#)
- [AML Template for Small Firms](#)

FINRA updated the AML Template for Small Firms to reflect new FINRA Rule 3310 and provided a new three-part podcast series to inform firms of those updates.

- [Anti-Money Laundering Template \(Part 1\)](#)
[Listen Now/Download | 11 min. 45 sec.](#)
- [Anti-Money Laundering Template \(Part 2\)](#)
[Listen Now/Download | 10 min. 35 sec.](#)
- [Anti-Money Laundering Template \(Part 3\)](#)
[Listen Now/Download | 10 min. 42 sec.](#)

The SEC updated the AML Source Tool to include guidance on the scope of permissible information sharing covered by Section 314(b), the Safe Harbor of the USA PATRIOT Act (June 2009).

- [SEC AML Source Tool](#)

SEC Suspicious Activity Report Alert Message Line

The SEC maintains a Suspicious Activity Report (SAR) Alert Message Line that securities firms can use to voluntarily report the filing of a SAR that may require



the SEC's immediate attention. Placing a call to the SEC SAR Alert Message Line does not alleviate a firm's obligation to file a SAR or notify an appropriate law enforcement authority.

- [SEC AML Source Tool](#)

***(Updated)* ARBITRATION RULES**

The following amendments to the Customer and Industry Codes of Arbitration apply to claims filed on or after January 18, 2010:

- clarification of the definition of "associated person" and conforming it to the FINRA By-Laws;
 - streamlining a case administration procedure; and
 - clarification that customers could be assessed hearing session fees based on their own claims for relief in connection with an industry claim.
- [FINRA Regulatory Notice 09-74](#): SEC Approves Changes to Arbitration Rules on Definition of Associated Person, Distribution of the FINRA Discovery Guide and Applicability of Hearing Session Fees (December 2009)

On March 22, 2010, the Codes of Arbitration Procedure for Customer and Industry disputes were amended to clarify that if a claim deficiency is corrected within 30 days from the time a party receives notice of a deficiency, the claim will be considered filed on the date the initial statement of claim was filed.

- [FINRA Regulatory Notice 10-11](#): Amendments to the Arbitration Rules Regarding Deficient Claims (March 2010)

***(New)* Non-Party Witness' Attorney May Attend Hearing While Witness Is Testifying**

Effective October 14, 2010, a non-party witness' attorney may attend an arbitration hearing while the witness is testifying. Unless otherwise authorized by the arbitrators, the attorney's role will be limited to asserting recognized privileges, such as the attorney-client and work-product privileges, and the



privilege against self-incrimination. The amendments to the Custom er and Industry Codes of Arbitration Procedure apply to all hearings taking place on or after October 14, 2010.

- [FINRA Regulatory Notice 10-40](#): Non-Party Witness' Attorney May Attend Hearing While Witness Is Testifying; Effective Date: October 14, 2010 (September 2010)

(New) Change to Expedited Proceedings for Failure to Comply With an Arbitration Award or Related Settlement

Firms and associated persons cannot rely on an inability-to-pay defense in expedited actions for failure to comply with arbitration awards involving customers if the FINRA Rule 9554 notice initiating the action was sent on or after July 2, 2010.

- [FINRA Regulatory Notice 10-31](#): Change to Expedited Proceedings for Failure to Comply with an Arbitration Award or Related Settlement (June 2010)

(New) Increase in Number of Arbitrators Available for Review When Parties Choose Arbitration Panels

On September 27, 2010, FINRA began increasing the number of proposed arbitrators available for review when parties choose arbitration panels from lists generated randomly by the Neutral List Selection System (NLSS). The amendments to the Custom er and Industry Codes of Arbitration Procedure (Codes) will apply to lists generated on or after the effective date.

- [FINRA Regulatory Notice 10-37](#): Increase in Number of Arbitrators Available for Review When Parties Choose Arbitration Panels (August 2010)

BUSINESS CONTINUITY

In August 2009, the SEC approved the adoption of NASD Rules 3510 (Business Continuity Plans) and 3520 (Emergency Contact Information) without significant change into the Consolidated FINRA Rulebook as FINRA Rule 4370 (Business Continuity Plans and Emergency Contact Information). FINRA Rule 4370,



however, modifies the requirement in NASD Rule 3520 that a firm designate two emergency contact persons who are both registered principals and members of senior management to require that only one of those associated persons be a member of senior management and a registered principal of the firm.

The rule also requires that someone designated as a second emergency contact person who is not a registered principal must be a member of senior management who has knowledge of the firm's business operations. Additionally, if a firm has only one associated person (e.g., a sole proprietorship without any other associated persons), FINRA Rule 4370 permits the second emergency contact person to be an individual, either registered with another firm or nonregistered, who has knowledge of the firm's business operations, such as the firm's attorney, accountant or clearing firm contact. FINRA Rule 4370 took effect on December 14, 2009.

- [FINRA Regulatory Notice 09-60](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules (October 2009)

***(Updated)* Business Continuity Planning**

Business continuity remains a priority for firms and their associated persons. It is important that firms maintain adequate business continuity and contingency plans, and ensure that employees are aware of and understand these plans.

- [FINRA Industry Issues Center - Business Continuity Planning](#)

A new podcast describes FINRA's Business Continuity Planning (BCP) Template and details recent updates, including those that were made to reflect FINRA's BCP Rule.

- [FINRA's Business Continuity Planning Template](#)
Listen Now/Download | 7 min. 30 sec.

COMMUNICATIONS WITH THE PUBLIC

Blogs and Social Networks

Americans are increasingly using social media websites, such as blogs and social networking sites, for business and personal communications. FINRA provides guidance to firms on how FINRA's communications with the public rules apply to



social media sites sponsored by a firm or registered representative. The guidance covers recordkeeping, suitability, supervision and other compliance concerns.

- [FINRA Regulatory Notice 10-06](#): Guidance on Blogs and Social Networking Web Sites (January 2010)

FINRA offers a podcast on social networking providing guidance on firms' use of blogs and social networking sites for business communications.

- [FINRA Compliance Podcast: Social Networking](#)
Listen Now/Download | 10 min. 52 sec.

In addition, FINRA offers two on-demand webinars on social networking:

- [Compliance Considerations for Social Networking Sites](#)
- [Implementing Compliance Practices for Social Networking Sites](#)

Electronic Communications

Firms are reminded to maintain and preserve all required communications, comply with recordkeeping requirements regarding external and internal communications, and address supervision, maintenance, retrieval and production issues, especially in light of the ever-increasing volume of data and methods of communication.

- [FINRA Regulatory Notice 07-59](#): FINRA Provides Guidance Regarding the Review and Supervision of Electronic Communications (December 2007)
- [FINRA Issue Center: Advertising](#): Guide to the Internet for Registered Representatives

Market Letters

Firms are permitted to supervise "market letters" as correspondence rather than sales literature, unless the letters were distributed to 25 or more existing retail customers within a 30-calendar-day period and make a financial or investment recommendation, or otherwise promote the firm's product or service.



- [FINRA Regulatory Notice 09-10](#): SEC Approves Rule Relating to Supervision of Market Letters (February 2009)

SIPC Information

Subject to certain exceptions, FINRA Rule 2266 (SIPC Information) requires firms to advise all new customers, in writing at the opening of an account, that they may obtain information about SIPC, including the SIPC brochure, by contacting SIPC. Such firms also must provide SIPC's website address and telephone number. In addition, firms must provide all customers with the same information, in writing, at least once each year. FINRA Rule 2266 took effect on August 17, 2009.

- [FINRA Regulatory Notice 09-33](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules (June 2009)

***(Updated)* CONSOLIDATED FINRA RULEBOOK**

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 (the Consolidated FINRA Rulebook). FINRA has been proposing new consolidated rules in phases for approval by the SEC as part of the Consolidated FINRA Rulebook. FINRA announces the effective dates for all new consolidated FINRA rules in *Regulatory Notices*. See the following *Notices* for the effective dates of new consolidated FINRA rules that the SEC has approved since the Spring 2010 Firm Element Advisory.

- [FINRA Regulatory Notice 10-35](#): SEC Approval and Effective Date for New Consolidated FINRA Rule (FINRA Rule 4320 (Short Sale Delivery Requirements)); Effective Date: October 15, 2010 (August 2010)
- [FINRA Regulatory Notice 10-21](#): SEC Approval and Effective Date for New Consolidated FINRA Rules and the Repeal of Certain NASD and Incorporated NYSE Rules; Effective Date: June 14, 2010 (April 2010)



Rule Conversion Charts

To facilitate the transition to the Consolidated FINRA Rulebook, FINRA created three rule conversion charts that map NASD and incorporated NYSE rules to new FINRA rules and vice versa. FINRA updates these charts as the effective dates of FINRA rules are announced.

Important Note: These conversion charts are intended as reference aids only and do not serve as substitutes for diligent review of the relevant rule language.

- [FINRA Rule Conversion Charts](#)

CORPORATE FINANCE AND INSTITUTIONAL BUSINESS

Member Private Offerings

FINRA reminds broker-dealers of their obligation to conduct a reasonable investigation of the issuer and the securities they recommend in offerings made under SEC Regulation D under the Securities Act of 1933—also known as private placements.

- [FINRA Regulatory Notice 10-22](#): Obligation of Broker-Dealers to Conduct Reasonable Investigations in Regulation D Offerings (April 2010)

Firms and associated persons that engage in a private placement of the firm's securities or those of a control entity must comply with certain disclosures and filing requirements and limitations of the use of proceeds as set forth in FINRA Rule 5122.

- [FINRA Regulatory Notice 09-27](#): SEC Approves New FINRA Rule 5122 Relating to Private Placements of Securities Issued by a Member Firm or a Control Entity (May 2009)



Resales of Unregistered Restricted Securities

Firms that participate in unregistered resales of restricted securities are reminded of their responsibilities to comply with certain federal securities laws and FINRA rules.

- [**FINRA Regulatory Notice 09-05**](#): FINRA Reminds Firms of Their Obligations to Determine Whether Securities are Eligible for Public Sale (January 2009)

(New) Processing of Company-Related Actions

On September 27, 2010, new FINRA Rule 6490 (Processing of Company-Related Actions) codified the requirements in Exchange Act Rule 10b-17 for issuers of a class of publicly trading securities to provide timely notice to FINRA of certain corporate actions (*e.g.*, dividend or other distribution of cash or securities, stock split or reverse split, rights or subscription offering). Issuers must also provide timely notification to FINRA of certain other specified corporate actions. Issuers must complete the necessary forms and pay the applicable fees within the required time periods or they will be subject to late fees and delayed processing of documents to announce corporate actions.

- [**FINRA Regulatory Notice 10-38**](#): SEC Approves New FINRA Rule Relating to the Processing of and Fees for Company-Related Actions for Non-Exchange-Listed Securities (August 2010)

CUSTOMER ACCOUNTS

(New) Providing Customers With Consolidated Financial Reports

The practice of providing customers with consolidated financial account reporting has become increasingly common in the financial services industry. In many cases, these reports offer a single document that combines information regarding most or all of the customer's financial holdings, regardless of where those assets are held. Firms are reminded that these reports represent communications with the public by the firm; the dissemination of these reports must comply with all applicable FINRA rules as well as the federal securities laws.



- [FINRA Regulatory Notice 10-19](#): FINRA Reminds Firms of Responsibilities When Providing Customers with Consolidated Financial Account Reports (April 2010)

FINRA released a podcast that offers guidance on consolidated account reports, including applicable rules and other considerations.

- **FINRA Compliance Podcast: Consolidated Account Reports**
[Listen Now/Download](#) | 10 min. 51 sec

(New) Master and Sub Accounts

FINRA reminds firms that maintain master/sub-account arrangements that, depending on the facts and circumstances of such arrangements, a firm may be required to recognize the sub-accounts as separate customer accounts for the purposes of applying FINRA rules, the federal securities laws and other applicable federal laws.

- [FINRA Regulatory Notice 10-18](#): FINRA Issues Guidance on Master and Sub-Account Arrangements (April 2010)

Federal Trade Commission's Red Flags Rule

The Federal Trade Commission's (FTC) Red Flags Rule, which implements obligations imposed by the Fair and Accurate Credit Transactions Act of 2003 (FACT Act), requires certain firms to create a written Identity Theft Prevention Program (ITPP) that is designed to identify, detect and respond to "red flags"—patterns, practices or specific activities—that could indicate identity theft. FINRA has developed an optional template that firms can use as a guide when fulfilling their requirements under the FTC's Red Flags Rule. The FTC has delayed enforcement of its Red Flags Rule until December 31, 2010.

- [FINRA Information Notice 7/1/09](#): Optional FTC Red Flags Rule Template
- [FINRA Regulatory Notice 08-69](#): Alert to Member Firms About the Federal Trade Commission's FACT Act Regulations and the Announcement of the FTC's Decision to Delay Enforcement of the Red Flags Rule (November 2008)



- [FINRA Issue Center: Customer Information Protection](#)
- [Federal Trade Commission](#): Fighting Fraud with the Red Flags Rule: A How-To Guide for Business (March 2009)

FINANCE AND OPERATIONS

Consolidated Financial Responsibility Rules

FINRA adopted a new set of financial responsibility rules for the Consolidated FINRA Rulebook. FINRA Rules 4110, 4120, 4130, 4140 and 4521 are new consolidated rules governing financial responsibility that are based in part on, and replace, provisions in the NASD and Incorporated NYSE Rules. FINRA also amended FINRA Rules 9557 and 9559 to, among other things, provide firms served with a notice under the financial responsibility rules an expedited appeal process, and made certain conforming revisions to Section 4(g) of Schedule A to the FINRA By-Laws. These changes took effect on February 8, 2010. (*See also* Customer Margin Balance Form and Subordinations below.)

- [FINRA Regulatory Notice 09-71](#): SEC Approves Consolidated FINRA Rules Governing Financial Responsibility (December 2009)

Financial Statements

Firms are reminded that their auditor must be registered with the Public Company Accounting Oversight Board (PCAOB). Since the SEC registration relief expired December 31, 2008, firms must file financial statements certified by a PCAOB-registered auditor for their fiscal years ending after that date. Firms are further reminded FINRA will treat financial statements certified by an auditor that is not PCAOB-registered as not having been filed under Section 4(g) of Schedule A to the FINRA By-Laws.

- [FINRA Information Notice 12/9/2009](#): Certification of Annual Audits
- [FINRA Information Notice 1/8/2009](#): Public Company Accounting Oversight Board Relief Expired December 31, 2008



FDIC Guaranteed Debt

FINRA advised firms of the Net Capital and Reserve Formula treatment of senior unsecured debt securities issued under the Debt Guarantee Program component of the Federal Deposit Insurance Corporation's (FDIC) Temporary Liquidity Guarantee Program.

- [FINRA Regulatory Notice 09-38](#): Guidance on the Net Capital and Reserve Formula Treatment of Senior Unsecured Debt Securities Issued Under the Debt Guarantee Program Component of the FDIC's Temporary Liquidity Guarantee Program (July 2009)

(New) Subordinations

In March 2010, FINRA reminded firms that, pursuant to new FINRA Rule 4110(e)(1), subordinated loans and notes collateralized by securities (together referred to as subordinations) must be approved by FINRA in order to receive beneficial regulatory capital treatment. FINRA explained the requirements for all subordinations for which firms intend to receive beneficial regulatory capital treatment (including certain provisions that all such subordinations, both standard and non-standard, must contain) and described the submission and approval process of proposed subordinations. FINRA also provided information about new, standard subordination forms (and a revised Lender's Attestation) that are available at www.finra.org/subordinations and explained how to obtain approval of proposed amendments to or renewals of previously approved subordinations. (See also Consolidated Financial Responsibility Rules above.)

- [FINRA Regulatory Notice 10-15](#): FINRA Requirements for Subordinations; Availability of New Standard Forms (March 2010)

INSURANCE/ANNUITIES

Deferred Variable Annuities

FINRA's deferred variable annuities rule (Rule 2330) establishes broker recommendation requirements (including suitability and disclosure obligations), principal review requirements, supervisory procedure requirements and training requirements. The implementation date of the FINRA rule—as well as previously approved amendments to parts of the rule covering principal review and supervisory procedures—was February 8, 2010. *Regulatory Notice 10-05*



addresses issues raised about a firm's ability to hold checks made payable to entities other than itself (third parties) pursuant to interpretive relief that FINRA previously issued.

- [FINRA Regulatory Notice 10-05](#): FINRA Reminds Firms of Their Responsibilities Under FINRA Rule 2330 for Recommended Purchases or Exchanges of Deferred Variable Annuities (January 2010)

A more in-depth discussion of the amendments regarding principal review and supervisory procedures under the rule on deferred variable annuities is provided in *Regulatory Notice 09-32*. Among other things, the amendments limited the rule's application to recommended transactions, changed the triggering event that begins the principal review period and clarified various other issues through supplementary material to the rule.

- [FINRA Regulatory Notice 09-32](#): SEC Approves Amendments to NASD Rule 2821 Governing Purchases and Exchanges of Deferred Variable Annuities (June 2009)
- [FINRA Regulatory Notice 09-72](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules (December 2009)
- [FINRA Issue Center](#): Variable Annuities

Variable Contracts

FINRA Rule 2320 regulates member firms in connection with the sale and distribution of variable life insurance and variable annuity contracts (together, variable contracts). It prohibits firms from participating in the offer or sale of a variable contract unless certain conditions are met. It also regulates member compensation in connection with the sale and distribution of variable contracts, including both cash and non-cash compensation arrangements.

- [FINRA Regulatory Notice 09-50](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules (September 2009)

Variable Life Settlements

Sales of existing life insurance policies to third parties are often referred to as "life settlements." Firms and associated persons are reminded that life settlements



involving variable insurance policies are securities transactions, and firms and associated persons involved in such transactions are subject to applicable FINRA rules.

- [FINRA Regulatory Notice 09-42](#): FINRA Reminds Firms of Their Obligations With Variable Life Settlement Activities (July 2009)

***(Updated)* MARGIN AND MARGIN ACCOUNTS**

On August 23, 2010, FINRA began introducing a new Regulatory Extension (REX) system that replaces FINRA's existing Reg T system to collect Regulation T and Exchange Act Rule 15c3-3 extension of time requests. Effective August 23, 2010, clearing firms must submit their monthly reporting of correspondent firms' extensions to transaction ratio by completing an online form accessible via the FINRA Firm Gateway through the new REX system. FINRA has revised the layout of the form, but it is otherwise unchanged. The new REX system also has new and modified data elements. On November 8, 2010, firms must submit all batch file extension of time requests via the new REX batch format, and the new and modified data elements will be required from all batch submitters.

- [FINRA Regulatory Notice 10-28](#): New System for Processing Regulation T and SEA Rule 15c3-3 Extension of Time Requests; Effective Dates: August 23, 2010 (Phase I); November 8, 2010 (Phase II) (June 2010)

Customer Margin Balance Form

In February 2010, FINRA announced that, beginning March 1, 2010, members subject to new FINRA Rule 4521(d) are required to file FINRA's new Customer Margin Balance Form. FINRA reminded firms that FINRA Rule 4521(d) governs filing requirements for customer margin accounts. The rule, adopted as part of the new consolidated financial responsibility rules, replaces Incorporated NYSE Rules 421(2) and 421.40 and applies to all FINRA members that carry customer margin accounts. (*See also* Consolidated Financial Responsibility Rules above.)

- [FINRA Regulatory Notice 10-08](#): Filing Requirements for Members that Carry Customer Margin Accounts; New Customer Margin Balance Form (February 2010)



Alternative Margin Treatment for Call Writes Against Employee Stock Options

On June 17, 2009, the SEC approved CBOE customer margin rules that provide for spread margin treatment on the writing of listed equity call options when, for the same underlying security and underlying quantity of shares, the writer owns employee stock options that are vested and exercisable.

- [CBOE Regulatory Circular RG09-141](#): Alternative Margin Treatment Available for Writing Listed Equity Call Options Against Employee Stock Options (December 2009)

Margin Requirements for Leveraged ETFs

The customer margin requirements for leveraged ETFs increased on December 1, 2009. And the customer margin requirements for uncovered options overlying leveraged ETFs, as well as the application of day-trading margin requirements for leveraged ETFs, increased on April 30, 2010.

- [FINRA Regulatory Notice 09-65](#): FINRA Delays the Effective Date for Increased Margin Requirements for Options on Leveraged ETFs and Day-Trading Requirements for Leveraged ETFs (November 2009)
- [CBOE Regulatory Circular RG09-132](#): Update of RG09-097, Margin Requirements for Leveraged ETFs and Uncovered Options on Leveraged ETFs (November 2009)
- [CBOE Regulatory Circular RG09-097](#): Margin Requirements for Leveraged ETFs and Uncovered Options on Leveraged ETFs (August 2009)
- [FINRA Regulatory Notice 09-53](#): Increased Margin Requirements for Leveraged Exchange-Traded Funds and Associated Uncovered Options (August 2009)

Margin Requirements for Credit Default Swaps

In May 2009, the SEC approved FINRA Rule 4240, which established an interim pilot program (the Interim Pilot Program) with respect to margin requirements for transactions in credit default swaps (CDS) executed by members. The rule, which went into effect on June 3, 2009, also sets forth risk monitoring procedures and



guidelines. The Interim Pilot Program's requirements extend to any transactions in CDS executed by a member firm (regardless of the type of account in which the transaction is booked), including those in which the offsetting matching hedging transactions are effected by the firm in CDS contracts that are cleared through the central counterparty clearing services of the Chicago Mercantile Exchange (CME). The Interim Pilot Program is in effect through November 30, 2010 (pursuant to SR-FINRA-2009-063, the program was extended from the original expiration date of September 25, 2009).

- [FINRA Regulatory Notice 09-30](#): SEC Approves Rule Establishing an Interim Pilot Program on Margin Requirements for Transactions in Credit Default Swaps (June 2009)

MUNICIPAL SECURITIES

***(Updated)* Auction Rate Securities**

In light of downgrades of municipal bond insurers, other short-term liquidity concerns creating extreme market volatility for municipal and other auction rate securities (ARS), an unprecedented number of "failed auctions" and several settlements, FINRA and the MSRB issued several notices pertaining to disclosures, margin, transaction reporting, reporting of customer complaints, suitability requirements and appropriate allocation procedures when a partial redemption of ARSs or other securities will occur.

- [FINRA Regulatory Notice 09-12](#): Reporting Requirements for Settlements of Customer Disputes Involving Auction Rate Securities (February 2009)
- [MSRB Notice 2008-36](#): Transaction Reporting of Dealer Buybacks of Auction Rate Securities: Rule G-14 (September 2008)
- [FINRA Regulatory Notice 08-21](#): FINRA Issues Guidance to Broker-Dealers on Partial Redemptions of Auction Rate Securities (April 2008)
- [MSRB Notice 2008-09](#): Application of MSRB Rules to Transactions in Auction Rate Securities (February 2008)

In 2009, the SEC approved amendments to MSRB Rule G-34 and MSRB Rule G-8 that require firms to report the reset interest rate and other descriptive information regarding ARS and variable rate demand obligations (VRDOs) to the



MSRB using the MSRB electronic system, the Short Term Obligation Rate Transparency System (SHORT). Additional amendments adopted in August 2010 require dealers to make additional submissions and disclosures regarding ARS and VRDOs (e.g., documents that define auction procedures and interest rate setting mechanisms for ARSs and liquidity facilities for VRDOs; ARS bidding information; additional VRDO information; minimum and maximum rates, etc.). Also, a dealer must communicate to an ARS Program Dealer if an order submitted for the auction is for an ARS issuer or conduit borrower. All information and documents are submitted to SHORT, and information becomes publicly available on the Electronic Municipal Market Access (EMMA) service. The effective date will be no later than May 20, 2011.

- [MSRB Notice 2010-31](#): SEC Approves Additional Increases in Transparency of Municipal Auction Rate Securities and Variable Rate Demand Obligations (August 2010)
- [MSRB Notice 2009-04](#): SEC Approves Proposal to Increase Transparency of Auction Rate Securities and Variable Rate Demand Obligations (January 2009)

On April 28, 2009, the MSRB filed a rule change for immediate effectiveness amending MSRB Rule G-8 that requires dealers involved in ARSs and VRDOs to keep specific additional records regarding such activities and SHORT reporting.

- [MSRB Notice 2009-16](#): Notice of Filing of Amendment to Rule G-8, On Books and Records, Relating to Auction Rate Securities and Variable Rate Demand Obligations (April 2009)
- [MSRB Notice 2008-04](#): Bond Insurance Ratings—Application of MSRB Rules (January 2008)

(Updated) Electronic Municipal Market Access System

The MSRB's all-electronic facility, EMMA, serves as a repository for primary market disclosure information, continuing disclosures and transaction information for the municipal securities market, and provides free public access to such information. Since June 1, 2009, underwriters submit all official statements (OSs) and advance refunding documents (ARDs) to the MSRB pursuant to revised Rule G-32, and any other disclosures in connection with primary offerings, which



become available on EMMA. Under certain circumstances, an underwriter's obligation to deliver an official statement to a customer who purchases municipal securities may be satisfied if the underwriter has made required submissions to EMMA.

Effective July 1, 2009, the MSRB modified EMMA to begin accepting continuing disclosure documents and related information from issuers and obligated persons pursuant to continuing disclosure undertakings entered that are consistent with Exchange Act Rule 15c2-12. EMMA also began accepting other continuing disclosures submitted on a voluntary basis by issuers and obligated persons.

On June 2, 2010, the SEC approved amendments to EMMA to permit issuers, on a voluntary basis, to submit to EMMA:

- preliminary official statements and other related pre-sale documents;
- official statements and advance refunding documents (primary market documents);
- information relating to the preparation and submission of audited financial statements;
- annual financial information; and
- to include hyperlinks to other disclosure information available from the issuer's website.

The effective date will be no later than May 26, 2011.

On June 2, 2010, the SEC approved amendments to MSRB Rule G-32 requiring brokers, dealers and municipal securities dealers acting as underwriters, placement agents or remarketing agents for primary offerings to provide EMMA information about whether the issuer or other obligated person has undertaken to provide continuing disclosures, the identity of any obligated persons other than the issuer, and the issuer's deadline for providing annual financial and operational information. The requirements will be effective no later than May 26, 2011.

On August 27, 2010, the MSRB announced that EMMA would be expanded to collect from issuers additional continuing disclosures the SEC added to Exchange Act Rule 15c2-12. The amendments to Exchange Act Rule 15c2-12 increased the list of specific events, such as bankruptcy or insolvency, mergers, acquisitions and similar events, for which a notice must be filed under Rule 15c2-12, and eliminated an exemption from the continuing disclosure provisions for dem and



securities, such as VRDOs. Beginning December 10, 2010, EMMA will accept submissions and make publicly available continuing disclosures containing such information.

EMMA is accessible at www.msrb.org or www.emma.msrb.org.

- [MSRB Notice 2010-32](#): MSRB Receives Approval to Modify the Continuing Disclosure Service of EMMA (August 2010)
- [MSRB Notice 2010-19](#): Reminder on Submission of Disclosure Documents to EMMA for 529 College Savings Plans (June 2010)
- [MSRB Notice 2010-15](#): MSRB Receives SEC Approval to Make Available Primary Market and Continuing Disclosure Information on EMMA (June 2010)
- [MSRB Notice 2009-39](#): MSRB Launches the Continuing Disclosure Service of its Electronic Municipal Market Access (EMMA) (July 2009)
- [MSRB Notice 2009-28](#): MSRB Establishes Electronic Official Statement Dissemination Standard under Rule G-32 and Launches Permanent Primary Market Disclosure Service of EMMA (June 2009)

***(Updated)* Municipal Securities Sales Practice and Supervisory Requirements**

In September 2010, the MSRB and FINRA jointly issued guidance reminding firms of a broad range of sales practice and supervisory obligations. Brokers, dealers and municipal securities dealers must fully understand the bonds they sell in order to meet their disclosure, suitability and pricing obligations under the rules of the MSRB and the federal securities laws. Dealers must obtain, analyze and disclose all material facts about the secondary market transactions that are known to the dealer, or are reasonably accessible to the market. Although EMMA provides a significant amount of important information about an issuer and a security, firms also may have a duty to obtain and disclose information that is not available through EMMA. Public availability of the information does not relieve a firm of its duty to disclose that information. Firms must perform an independent analysis of the bonds they sell, and may not rely solely on a bond's credit rating. Firms also must use available information to establish a fair price in transactions with customers. Supervision and monitoring of supervisory systems are also discussed.



- [MSRB Notice 2010-37](#): MSRB Reminds Firms of their Sales Practice and Due Diligence Obligations When Selling Municipal Securities in the Secondary Market (September 2010)
- [FINRA Regulatory Notice 10-41](#): FINRA Reminds Firms of Their Sales Practice and Due Diligence Obligations When Selling Municipal Securities in the Secondary Market (September 2010)

FINRA has designed the [Municipal Bond Sales in the Secondary Market: Checklist for Customer Disclosure](#) — a voluntary tool that provides guidance to firms with respect to their customer disclosure obligations.

FINRA offers a [podcast](#) on sales practice and due diligence obligations regarding municipal securities transactions.

- [FINRA Compliance Podcast: Municipal Securities \(Part I of III\)](#)
Listen Now/Download | 7 min. 45 sec

FINRA also is hosting a [webinar](#) on disclosure and enforcement trends in municipal securities on November 17, 2010. An on-demand version of this webinar will be available at a later date.

- [Municipal Securities Compliance and Enforcement Priorities: Disclosures and Other Enforcement Trends](#): November 17, 2010

FINRA offers an on-demand webinar regarding pricing issues with municipal securities.

- [Municipal Securities Compliance and Enforcement Priorities: Pricing Issues](#)

In July 2009, the MSRB discussed a firm's sales practice obligations, including a dealer's obligation under MSRB Rule G-17 to disclose to a customer all material information about a transaction known by the dealer as well as material information about the security that is reasonably accessible to the market. With the advent of EMMA and price transparency, the flow of information (amount, nature, timing and accessibility) has improved, requiring review of a dealer's practices, policies and procedures.



- [MSRB Notice 2009-42](#): MSRB Issues Interpretive Guidance on Disclosure and Other Sales Practice Obligations to Individual and Other Retail Investors in Municipal Securities (July 2009)

FINRA recommends that firms engaged in municipal securities business review and, if necessary, modify their existing policies and procedures to comply with changes in the MSRB EMMA system and changes to MSRB rules.

- [FINRA Regulatory Notice 09-35](#): FINRA Recommends Review of Municipal Securities Activities (June 2009)

***(Updated)* New Issue Municipal Securities**

The American Recovery and Reinvestment Act of 2009 added provisions to the Internal Revenue Code authorizing state and local governments to issue two types of Build America Bonds: Build America Bonds (Tax Credit) and Build America Bonds (Direct Payment). Since these bonds are municipal bonds, dealers engaged in municipal securities business activities in connection with these bonds are subject to all MSRB rules, including appropriate professional qualifications and supervision, underwriting, reporting, confirmation of transactions to customers, political contributions, the payment of MSRB underwriting and transaction assessment fees, automated clearance and settlement, etc. With regard to political contributions, dealers may wish to note that the making of presentations to potential issuers of Build America Bonds or other tax credit bonds would be considered a solicitation of municipal securities business. Personnel participating in such activity would be considered municipal finance professionals of the dealer under Rule G-37, even if such personnel are employed in divisions or departments of the dealer that do not traditionally engage in municipal securities business.

- [MSRB Notice 2009-15](#): Build America Bonds and Other Tax Credit Bonds (April 2009)
- [MSRB Notice 2009-30](#): Application of Rule G-37 to Solicitations of Issuers (June 2009)
- [MSRB Notice 2009-49](#): Build America Bonds: Reminder of Rule G-15(A) Customer Confirmation Yield Disclosure Requirement (August 2009)

The MSRB reminds dealers that they must comply with the fair practice obligations under MSRB Rule G-17 in their municipal securities activities with



issuers of municipal securities. The duty to an issuer extends to all municipal securities activities, such as representations made to an issuer regarding investors during an underwriting (e.g., regarding retail investors and retail order periods), and certain payments made and expenses reimbursed for excessive or lavish entertainment or travel expenses in connection with an issuance.

- [MSRB Notice 2009-54](#): Reminder Notice of Fair Practice Duties to Issuers of Municipal Securities (September 2009)

On October 13, 2010, MSRB Rule G-11 was amended to apply to all primary offerings, whether or not a syndicate has been formed, and to improve the distribution of new issues by ensuring that underwriters follow the priority provisions in the offering. Underwriters are required to give priority to customer orders over orders for their own or related accounts to the extent consistent with orderly distribution or unless otherwise agreed to by the issuer, and must keep additional records regarding underwriting and trading accounts. Concurrently approved MSRB interpretive guidance states that MSRB Rule G-17 requires underwriters to give customer orders priority unless specific exceptions apply, and it may be a violation of MSRB Rule G-17 if an underwriter fails to follow an issuer's directions concerning a retail order period.

- [MSRB Notice 2010-26](#): Priority of Orders in Primary Offerings Proposed Rule Change Approved (August 2010)

(New) Municipal Advisors

The Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) requires the registration of persons who are municipal advisors with the SEC by October 1, 2010. "Municipal advisor" is defined in Section 975 of the Dodd-Frank Act (and in Exchange Act Section 15B(e)(4)). The SEC issued an interim final temporary rule that establishes a means for municipal advisors to temporarily register before October 1, 2010. Temporary registration will expire December 31, 2011, and will be followed by a final SEC rule establishing the permanent requirements and process for registration of municipal advisors.



- [Exchange Act Release No. 62824](#) (September 1, 2010); 75 FR 54465 (September 8, 2010); amended Exchange Act Section 15B(e)(4), effective October 1, 2010.

***(Updated)* Political Contributions and the Solicitation of Municipal Securities Business**

In 2009, the MSRB published an interpretive letter regarding the activities of a broker-dealer that is engaged in soliciting municipal securities business on behalf of an affiliated company.

- [MSRB Notice 2009-40](#): MSRB Publishes Interpretive Letter Regarding Solicitation Activity on Behalf of an Affiliated Company Pursuant to Rules G-37 and G-38 (July 2009)

The SEC has approved changes to MSRB Rule G-37 that require the public disclosure of certain contributions made to bond ballot campaigns by dealers, their political action committees, municipal finance professionals (MFPs) and non-MFP executive officers. Dealers are also required to create and maintain records of contributions to bond ballot campaigns. The amendments became effective on February 1, 2010.

- [MSRB Notice 2010-01](#): SEC Approves Amendments to Rule G-37 and Rule G-8 Relating to Political Contributions (January 22, 2010)
- [Investment Advisers Act Release No. 3043](#) (July 1, 2010), 75 FR 41018 (July 14 2010)

OPTIONS

***(Updated)* Options Disclosure Document**

On May 24, 2010, the SEC approved a [supplement to the Options Disclosure Document](#) (ODD). The ODD contains general disclosures on the characteristics and risks of trading standardized options. The revised supplement adds disclosure regarding the characteristics of options on conventional index-linked securities, as well as the special risks of these options. The ODD is amended to include BATS



Exchange, Inc. and its corporate address to the front inside cover page of the ODD. As with other supplements to the ODD, this should be read in conjunction with the current ODD entitled Characteristics and Risks of Standardized Options.

- [FINRA Information Notice 09/07/2010](#): Supplement to the Securities Futures Risk Disclosure Document
- [FINRA Information Notice 06/15/2010](#): Supplement to the Options Disclosure Document
- [CBOE Regulatory Circular RG10-67](#): Supplement to the Options Disclosure Document

Options Communications Rules

FINRA Rule 2220 (Options Communications) adopted without substantive change NASD Rule 2220 (Options Communications) into the Consolidated FINRA Rulebook. FINRA Rule 2220 took effect on December 14, 2009. The SEC has also approved similar changes to CBOE Rule 9.21, Communications to Customers.

- [FINRA Regulatory Notice 09-60](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules (October 2009)
- [FINRA Regulatory Notice 08-73](#): SEC Approves Amendments to NASD Rule 2220 to Update the Standards for Options Communications, (December 2008)
- [CBOE Regulatory Circular RG08-155](#): Revisions to Options Communications Rules (November 2008)

***(Updated)* Standardized Options Exercise Procedures**

Effective September 7, 2010, amendments to FINRA Rule 2360 (Options) extend the cut-off time for the submission of certain contrary exercise advice by one hour to 7:30 p.m. Eastern Time. Additionally, in the event of a modified close of trading, the amendments extend the deadline for option holders to make a final exercise decision for an expiring standardized option by two minutes to one hour and 30 minutes following the modified closing time.



- [FINRA Regulatory Notice 10-36](#): Amendments to Standardized Options Exercise Procedures and Extension of Contrary Exercise Advice Cut-Off Time (August 2010)

REGISTRATION AND DISCLOSURE

(New) Changes to Customer Complaint Reporting Procedures

Since July 1, 2010, the beginning of the third calendar quarter, firms are required to use revised and new product codes to report statistical information regarding written customer complaints relating to annuities and life settlement products. The first report using the revised and new codes is due by October 15, 2010, which is the reporting deadline for customer complaints received during the third calendar quarter.

- [FINRA Regulatory Notice 10-27](#): Changes to Customer Complaint Reporting Procedures Under NASD Rule 3070(c) and NYSE Rule 351(d) (June 2010)

Eligibility Proceedings

The FINRA Rule 9520 Series sets forth eligibility proceedings under which FINRA may allow a person subject to a statutory disqualification to enter or remain in the securities industry. Amendments to the FINRA Rule 9520 Series address the circumstances under which persons subject to certain statutory disqualifications must obtain FINRA approval to enter or remain in the securities industry.

- [FINRA Regulatory Notice 09-19](#): Amendments to FINRA Rule 9520 Series to establish Procedures Applicable to Firms and Associated Persons Subject to Certain Statutory Disqualifications (April 2009)

(Updated) BrokerCheck[®] and Dispute Process

FINRA Rule 8312 governs the information FINRA releases to the public via BrokerCheck. FINRA Rule 8312 makes permanently available in BrokerCheck information concerning final regulatory actions against brokers—as well as certain administrative information (*e.g.*, employment and registration history) and information about qualification examinations, if available, and the broker's most



recently submitted comment, if any, regardless of when they were employed in the securities industry.

- [FINRA Regulatory Notice 09-66](#): SEC Approves Changes to FINRA's BrokerCheck Disclosure Rule to Retain and Make Publicly Available Information About Final Regulatory Actions Against Former Brokers (November 2009)

In July 2010, the SEC approved amendments to FINRA Rule 8312 to be implemented in phases. On August 23, 2010, the amendments:

- made publicly available in BrokerCheck all historic customer complaints that became non-reportable after the implementation of Web CRD in 1999; and
- codified FINRA's current process for disputing the accuracy of (or updating) information disclosed through BrokerCheck.

Effective November 6, 2010, the amendments will:

- expand the BrokerCheck disclosure period for former associated persons of a member firm to 10 years from two years; and
 - permanently make publicly available in BrokerCheck certain information about former associated persons of a firm if any of the following applies, as reported to CRD on a uniform registration form: (i) the person was convicted of or pled guilty or nolo contendere to a crime; (ii) the person was the subject of a civil injunction in connection with investment-related activity or a civil court finding or involvement in a violation of any investment-related statute or regulation; or (iii) the person was named as a respondent or defendant in an investment-related, consumer-initiated arbitration or civil litigation which alleged that the person was involved in a sales practice violation and which resulted in an arbitration award or civil judgment against the person.
- [FINRA Regulatory Notice 10-34](#): SEC Approves Changes to Expand the Information Released Through BrokerCheck and Establish a Process to Dispute (or Update) Information Disclosed Through BrokerCheck (July 2010)



FINRA reminded member firms of changes to BrokerCheck it implemented on August 23, 2010, and the steps firms and individuals could take with respect to the changes prior to implementation.

- [FINRA Information Notice 8/3/2010](#)

***(Updated)* Revised Forms U4 and U5**

Amendments to Forms U4 and U5 and FINRA Rule 8312 (FINRA BrokerCheck Disclosure) include, among other things, significant changes to disclosure questions on the Forms, including the addition of questions about certain regulatory actions; new questions that require firms to report allegations of sales practice violations made against a registered person in an arbitration or litigation in which the registered person is not a named party; and an increase in the monetary threshold for reporting settlements of customer complaints, arbitrations or litigations from \$10,000 to \$15,000. The amendments took effect on May 19, 2009, except for the disclosure questions regarding regulatory actions, which took effect on November 14, 2009.

- [FINRA Regulatory Notice 09-23](#): SEC Approval of Proposed Changes to Forms U4 and U5 and FINRA Rule 8312 (FINRA BrokerCheck Disclosure) (May 2009)

In September 2010, FINRA reminded firms about their obligation to provide timely, complete and accurate disclosure on Form U5.

- [FINRA Regulatory Notice 10-39](#): Obligation to Provide Timely, Complete and Accurate Information on Form U5 (September 2010)

In addition, FINRA offers a webcast that explains the process for submitting Form U4 and Form U5 filings.

- [What to Expect: The U4 and U5 Filing Process](#)

Record Retention Requirements for Uniform Forms

FINRA member firms can rely on Web CRD to satisfy their record retention requirements with respect to certain Forms U4, U5 and BR filed in Web CRD,



provided they adhere to the terms of the no-action relief granted by the staff of the SEC.

- [FINRA Information Notice 2/21/08](#): FINRA Secures Relief for Member Firms for Certain Record Retention Requirements (February 2008)

FINRA Rule 1010 (Electronic Filing Requirements for Uniform Forms) supports the information reported by firms to Web CRD and, among other things, permits firms to file amendments to Form U4 disclosure information without obtaining the associated person's manual signature, provided that the firm uses reasonable efforts to:

- provide the registered person with a copy of the amended disclosure information prior to filing; and
- obtain the registered person's written acknowledgment (which may be electronic) prior to filing that the information has been received and reviewed subject to certain specified conditions.

FINRA Rule 2263 (Arbitration Disclosure to Associated Persons Signing or Acknowledging Form U4) requires firms to provide each associated person with arbitration disclosures whenever the firm asks an associated person, pursuant to FINRA Rule 1010, to manually sign a new or amended Form U4, or to otherwise provide written acknowledgment of an amendment to the Form U4. FINRA Rule 1010 took effect on July 27, 2009 and FINRA Rule 2263 took effect on September 25, 2009.

- [FINRA Regulatory Notice 09-40](#): SEC Approval and Effective Dates for New Consolidated FINRA Rules on Electronic Filing Requirements for Uniform Forms and Arbitration Disclosures (July 2009)

RESEARCH

Trading Ahead of Research Reports

The SEC approved FINRA Rule 5280 (Trading Ahead of Research Reports) as part of the Consolidated FINRA Rulebook. The rule, which contains certain modifications to previous NASD Interpretive Material, became effective on April 20, 2009.

- [FINRA Regulatory Notice 09-11](#): SEC Approval and Effective Dates for



New Consolidated FINRA Rule on Trading Ahead of Research Reports
(February 2009)

SALES PRACTICE AND SUPERVISION

Annual Reporting

CBOE reminded its members and member firms of the requirement to submit a written report by April 1st of each year that details the firm's supervision and compliance effort and report on the firm's ongoing compliance processes and procedures.

- [**CBOE Regulatory Circular RG08-168**](#): Annual Reporting Pursuant to CBOE Rule 9.8 – Supervision of Accounts (December 2008)

Designations

Regulators have sought to address concerns relating to the proliferation of professional designations, including those that require no meaningful training or specialized knowledge but suggest an expertise in retirement planning or financial services for seniors.

- [**NASAA Model Rule**](#): Use of Senior-Specific Certifications and Professional Designations (March 2008)
- [**FINRA Regulatory Notice 07-43**](#): FINRA Reminds Firms of Their Obligations Relating to Senior Investors and Highlights Industry Practices to Serve these Customers (September 2007)
- [**FINRA Investor Information**](#): Understanding Professional Designations

SHORT SALES

Amendments to SEC Regulation SHO

On February 24, 2010, the SEC adopted amendments to Regulation SHO to, among other things, implement an alternative uptick rule (new Rule 201). Rule 201 imposes restrictions on short selling whenever the price of a covered security declines by 10 percent or more from the prior day's close, in which case a circuit breaker is triggered for that security restricting short sales at any price less than or equal to the current national best bid in that security for the remainder of the day



and the following day. The rule requires trading centers to establish, maintain and enforce written policies and procedures that are reasonably designed to prevent the execution or display of a prohibited short sale. Rule 201 took effect on May 10, 2010, with a compliance date of November 10, 2010.

Short Sales, Temporary Rule 204T of Regulation SHO Now Permanent

On July 27, 2009, the SEC issued an order making interim final temporary Rule 204T of Regulation SHO permanent, effective as of July 31, 2009 (the date on which Rule 204T was set to expire). Rule 204T sets out specific requirements to promptly purchase or borrow securities to deliver on long and short sales. The new rule (Rule 204) maintains the structure of Rule 204T with some modifications. In addition, the SEC's order notes that volume weighted average price (VWAP) orders may be utilized to close-out fails to deliver. A VWAP order must be irrevocable, received by no later than the beginning of regular trading hours on the applicable close-out date, have a final execution price that is determined after the close of regular trading hours when the VWAP value is calculated and be executed on an agency basis.

- [CBOE Regulatory Circular RG09-83](#): Short Sales, Temporary Rule 204T of Regulation SHO now permanent (August 11, 2009)
- [SEC Division of Market Regulation](#): Responses to Frequently Asked Questions Concerning Regulation SHO (Updated 8/28/2009)

TRADING PRACTICES AND SUPERVISION

***(Updated)* Clearly Erroneous Trades**

The FINRA Rule 11890 Series, governing clearly erroneous transactions, replaces NASD Rule 11890, IM-11890-1 and IM-11890-2 and was adopted as part of a market-wide effort by multiple SROs to provide transparency and finality with respect to clearly erroneous executions. Among other things, the rule series includes a new general rule defining "clearly erroneous" transactions, separate provisions for the determination of clearly erroneous transactions depending upon whether the transaction involves an exchange-listed security or an over-the-counter equity security and procedures for appealing FINRA clearly erroneous determinations. In addition, the rule series codifies minimum numerical criteria necessary for a transaction to qualify as clearly erroneous.



- [FINRA Regulatory Notice 10-04](#): SEC Approves Consolidated FINRA Rules Governing Clearly Erroneous Transactions (January 2010)

Effective September 10, 2010, FINRA amended Rule 11892 to refine and clarify the process for making clearly erroneous determinations for over-the-counter transactions in exchange-listed securities, including events involving trading pauses and multiple stocks. The amendments to Rule 11892 also, among other things, reduce the ability of FINRA to deviate from the objective standards set forth in the rule.

- [FINRA Regulatory Notice 10-43](#): Amendments to FINRA Rules on Trading Pauses Due to Extraordinary Market Volatility and Clearly Erroneous Transactions in Exchange-Listed Securities (September 2010)

Handling of Large Orders

NYSE Regulation issued regulatory guidance on supervising the handling of large orders, which can raise regulatory concerns. These concerns include potential conflicts of interest, best execution obligations, manipulation and special considerations relating to trading strategies and benchmarks revolving around the closing price of a security.

- [NYSE Regulation Information Memo 09-40](#): Regulatory Guidance on Handling of Large Orders (August 2009)

Indications of Interest

FINRA reminded firms of their obligations to communicate accurate information when disseminating, or using services to disseminate indications of interest to the marketplace.

- [FINRA Regulatory Notice 09-28](#): FINRA Reminds Firms of Their Obligations to Provide Accurate Information in Disseminating, or Using Services to Disseminate, Indications of Interest (May 2009)

TRANSACTION REPORTING AND DATA DISSEMINATION

Alternative Trading Systems

FINRA reminded firms that are alternative trading systems or operate alternative



trading systems that, in addition to filing all reports required by Regulation ATS with the SEC, they also must simultaneously file duplicate copies of most reports with FINRA.

- [FINRA Regulatory Notice 09-46](#): FINRA Reminds Alternative Trading Systems of Their Reporting Obligations (August 2009)

***(Updated)* Trade Reporting and Compliance Engine (TRACE)**

Effective February 14, 2011, the definition of TRACE-Eligible Security will be expanded to include Asset-Backed Securities, and firms trading Asset-Backed Securities must report their transactions to TRACE. “Asset-Backed Security” is broadly defined in Rule 6710(m), and included among the many types of securities are mortgage-backed securities and collateralized debt obligations.

- [FINRA Regulatory Notice 10-23](#): SEC Approves Reporting Asset-Backed Securities Transactions to TRACE and Related Fees (April 2010)

Effective March 1, 2010, the definition of TRACE-Eligible Security was expanded to include Agency Debt Securities, requiring firms to report transactions in such securities. For purposes of TRACE, Agency Debt Securities are debt securities that are issued or guaranteed by a U.S. agency (Agency) or a government-sponsored enterprise (GSE). The term Agency is broadly defined. Agency Debt Securities do not include U.S. Treasury securities. In addition, the amendments require firms to report primary market transaction in TRACE-Eligible Securities. Previously, firms were required to report secondary market transactions only.

- [FINRA Regulatory Notice 09-57](#): SEC Approves Amendments Expanding TRACE to Include Agency Debt Securities and Primary Market Transactions (September 2009)

Effective June 15, 2009, the definition of TRACE-Eligible Security was broadened to delete the following two requirements: (1) that TRACE-Eligible Securities be registered under the Securities Act of 1933; and (2) with respect to securities that are resold in a Securities Act Rule 144A transaction, that such securities initially be offered and sold under the exemption from registration in Section 4(2) of the Securities Act.



- [FINRA Regulatory Notice 09-24](#): SEC Approves Amendments Expanding the Definition of “TRACE-Eligible Security” (May 2009)

Trade Reporting Structure for Equity Securities

Effective August 3, 2009, firms' trade reporting obligations for over-the-counter (OTC) equity transactions were changed. Specifically, FINRA trade reporting rules were amended to (1) replace the current market maker-based trade reporting structure with an "executing party" structure; and (2) require firms with the trade reporting obligation that are acting in a riskless principal or agency capacity on behalf of another member firm(s) to submit non-tape report(s) to FINRA, as necessary, to identify such other firm(s) as a party to the trade.

- [FINRA Regulatory Notice 09-08](#): SEC Approves Amendments to FINRA Trade Reporting Rules (January 2009)

(New) Timely Trade Reporting

Effective November 1, 2010, firms are required to report OTC transactions in equity securities to FINRA within 30 seconds of execution. The new reporting time frame also applies to trade cancellations that currently are subject to 90-second reporting, as well as stop stock and prior reference price trades.

In addition, as part of the November 1, 2010 changes, firms are required to report secondary market transactions in non-exchange-listed direct participation program securities within 30 seconds of execution. Therefore, such transactions will be subject to regulatory transaction fees under Section 3 of Schedule A to the FINRA By-Laws.

- [FINRA Regulatory Notice 10-24](#): SEC Approves Amendments to Require Reporting of OTC Trades in Equity Securities Within 30 Seconds of Execution; Effective Date: November 1, 2010 (April 2010)

(New) OTC Equity and Restricted Securities

Firms must report transactions in restricted equity securities traded pursuant to SEC Rule 144A to the OTC Reporting Facility no later than 8 p.m. Eastern Time. These reporting requirements replace the trade reporting obligations for restricted equity securities in FINRA's PORTAL rules (FINRA Rule 6630 Series).



Additionally, FINRA changed the definition of "OTC Equity Security," which took effect on June 28, 2010. The amendments align the term "OTC Equity Security" more closely with SEC rule terminology and improve consistency across the FINRA rulebook. The amendments also clarify the application of the OTC Reporting Facility reporting requirements to transactions reported on or through an exchange.

- [FINRA Regulatory Notice 10-26](#): SEC Approves Amendments to Trade Reporting Requirements for Restricted Equity Securities and Revisions to the Definition of OTC Equity Security; Effective Date: June 28, 2010 (May 2010)

Firms must comply with amended rules on applicable trade report modifiers when reporting OTC transactions in non-NMS stocks to the OTC Reporting Facility.

- [FINRA Regulatory Notice 10-29](#): SEC Approves Amendments to Rules on Reporting Transactions to the OTC Reporting Facility; Effective Date: November 1, 2010 (June 2010)

Related Market Center

Effective May 3, 2010, firms must identify the Related Market Center in non-tape reports submitted to a FINRA trade reporting facility.

- [FINRA Trade Reporting Notice 2/8/10](#): FINRA Extends Implementation of Amendments Requiring Related Market Center Indicator in Non-Tape Reports Submitted to FINRA. (This *Notice* supplements, and should be read in conjunction with, *Regulatory Notice 09-54* (September 2009)).

(New) Trading Halts

FINRA began a pilot program in which it will halt trading otherwise than on an exchange with respect to securities included in the S&P 500® Index where the primary listing market has issued a trading pause due to extraordinary market volatility. The pilot is set to end on December 10, 2010.

- [FINRA Regulatory Notice 10-30](#): SEC Approves Amendments Permitting FINRA to Halt Trading by Firms Otherwise Than on an Exchange Where a Primary Listing Market Has Issued a Trading Pause



Due to Extraordinary Market Volatility; Effective Date: June 10, 2010
(June 2010)

Effective September 14, 2010, FINRA expanded the scope of the trading pause pilot program to halt trading otherwise than on an exchange with respect to securities included in the Russell 1000[®] Index and certain exchange-traded products. The expanded pilot is set to end on December 10, 2010.

- [FINRA Regulatory Notice 10-43](#) : Amendments to FINRA Rules on Trading Pauses Due to Extraordinary Market Volatility and Clearly Erroneous Transactions in Exchange-Listed Securities (September 2010)

Effective October 18, 2010, firms must use the weighted-average price/special pricing formula (W) trade modifier on trade reports submitted to the Alternative Display Facility or a Trade Reporting Facility reflecting the following types of trades: qualified contingent trades, error correction and print protection. Because these transactions are not necessarily based on the current market price of the security when reported, FINRA believes that they are not appropriate triggers for a trading pause and should be marked with the “W” trade modifier.

- [FINRA Trade Reporting Notice 8/19/10](#): Weighted-Average Price/Special Pricing Formula Trade Modifier

FINRA issued a Trade Reporting Notice to explain the price validation protocol of the FINRA trade reporting facilities and to set forth new guidance on the use of the price override indicator in trade reports. Firms are required to make systems changes necessary to report in accordance with the *Notice* no later than November 16, 2010.

- [FINRA Trade Reporting Notice 9/17/10](#): Price Validation and Price-Override Protocol



Trade Reporting Frequently Asked Questions

FINRA publishes on its website Trade Reporting Frequently Asked Questions (FAQ), which provide guidance for firms on reporting OTC transactions in equity securities to a FINRA Facility (*i.e.*, a Trade Reporting Facility (TRF), the Alternative Display Facility (ADF) or the OTC Reporting Facility (ORF)). Firms should be aware of and review these FAQs, which FINRA updates periodically.

- [FINRA Trade Reporting Notice 8/14/08](#): Trade Reporting Frequently Asked Questions



More Information and resources:

Contact CE Council members for more information:

Regulatory Organization	Web Site
Chicago Board Options Exchange	www.cboe.com
FINRA	www.finra.org
Municipal Securities Rulemaking Board	www.msrb.org
North American Securities Administrators Association	www.nasaa.org
U.S. Securities and Exchange Commission	www.sec.gov