

Personal Securities Transactions

FINRA Requests Comment on Proposed Consolidated FINRA Rule Governing Personal Securities Transactions for or by Associated Persons

Comment Period Expires: June 5, 2009

Executive Summary

As part of the process to develop a new consolidated rulebook (the Consolidated FINRA Rulebook),¹ FINRA is requesting comment on proposed new FINRA Rule 3210 (Personal Securities Transactions for or by Associated Persons). The proposed rule, which combines and streamlines certain provisions of NASD Rule 3050 and Incorporated NYSE Rule 407² in addition to adopting additional requirements, would promote more effective oversight of the personal trading activities of associated persons of member firms.³

This *Notice* also requests comment on how firms currently obtain information pursuant to NASD Rule 3050 or NYSE Rule 407, as applicable, and the processes and controls currently implemented upon receipt of such information.

The text of the proposed rule is set forth in Attachment A.

Questions regarding this *Notice* should be directed to Adam H. Arkel, Assistant General Counsel, Office of General Counsel, at (202) 728-6961.

April 2009

Notice Type

- Request for Comment
- Consolidated FINRA Rulebook

Suggested Routing

- Compliance
- Legal
- Senior Management

Key Topic(s)

- Personal Securities Transactions of Associated Persons
- Supervision

Referenced Rules & Notices

- NASD Rule 3040
- NASD Rule 3050
- NYSE Rule 407
- NYSE Rule Interpretation 407/01
- NYSE Rule 407A
- Regulatory Notice 08-24

Action Requested

FINRA encourages all interested parties to comment on the proposed rules. Comments must be received by June 5, 2009.

Member firms and other interested parties can submit their comments using the following methods:

- Emailing comments to *pubcom@finra.org*; or
- Mailing comments in hard copy to:

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, N.W.
Washington, D.C. 20006-1506

To help FINRA process and review comments more efficiently, persons should only use one method to comment on the proposal.

Important Notes: The only comments that FINRA will consider are those submitted pursuant to the methods described above. All comments received in response to this Notice will be made available to the public on the FINRA Web site. Generally, FINRA will post comments on its site one week after the end of the comment period.⁴

Before becoming effective, a proposed rule change must be authorized for filing with the SEC by the FINRA Board of Governors, and then must be approved by the SEC, following publication for public comment in the *Federal Register*.⁵

Background and Discussion

Sound supervisory practices require that a member firm monitor personal securities transactions that are effected outside of the firm by or for its associated persons.⁶ Currently, NASD Rule 3050 and NYSE Rule 407 address this subject matter. Proposed FINRA Rule 3210 combines and streamlines certain provisions of the NASD and NYSE rules and adopts additional requirements designed to promote more effective oversight of the personal trading activities of associated persons.

Prior Written Consent Requirement

Based in large part on NYSE Rule 407, proposed FINRA Rule 3210(a) prohibits any associated person, without the prior written consent of his or her employer (referred to as the employer member) from opening or otherwise establishing at another member firm (referred to as the executing member), or at any other financial institution,⁷ any account in which securities transactions can be effected⁸ and in which such associated person has a personal financial interest.⁹ (FINRA notes that, as a general matter, “personal financial interest” would extend to a spouse’s account.) The proposed rule further adds a new requirement that, as a condition to granting prior written consent, the employer member must instruct the associated person to have the executing member provide duplicate account statements and confirmations to the employer member.¹⁰ In addition, as discussed below, the proposed rule obligates the executing member to carry out the associated person’s instructions.

Notification by the Associated Person

Proposed FINRA Rule 3210(b) requires that any associated person, prior to opening or otherwise establishing an account pursuant to the rule, must notify in writing the executing member, or other financial institution, of his or her association with the employer member. This requirement is based in part on the associated person’s notification obligations under NASD Rules 3050(c) and (d). The proposed rule adds the requirement that the associated person must state in the notice provided to the executing member or other financial institution that he or she has a personal financial interest in the account.

Obligations of the Executing Member

Based in large part on NYSE Rule 407(a), proposed FINRA Rule 3210(c) requires that, when an executing member has actual notice that an associated person of an employer member has a personal financial interest in any account opened or otherwise established at the executing member, the executing member must not execute any securities transactions in that account unless it has obtained the employer member’s prior written consent. In addition, the proposed rule provides that the executing member must promptly obtain and implement an instruction from the associated person¹¹ directing that duplicate account statements and confirmations be provided to the employer member.¹²

Revocation of Employer Member's Consent

Proposed FINRA Rule 3210.04 sets forth a new requirement that, if an employer member does not receive the duplicate account statements and confirmations required pursuant to the rule in a timely manner, the employer member must revoke its consent to maintain the account and notify the executing member or other financial institution in writing of the revocation. The employer member would be required to obtain promptly records from the executing member that the account was closed.

Accounts Opened Prior to Association With an Employer Member

The proposed rule, similar to current provisions in NASD Rules 3050(c) and (d), makes allowance for accounts opened by an associated person prior to his or her association with the employer member. Specifically, proposed FINRA Rule 3210.01 provides that if the account was opened or otherwise established prior to association with the employer member, the associated person would be required, within fifteen business days of becoming associated, to obtain the employer member's consent to maintain the account and to notify in writing the executing member or other financial institution of his or her association with the employer member and personal financial interest. In addition, the proposed rule provides that the associated person must instruct the executing member or other financial institution to provide to the employer member duplicate account statements and confirmations as of the date of his or her association with the employer member.

Deleted Requirements

Proposed FINRA Rule 3210 deletes a number of requirements in NASD Rule 3050 and NYSE Rule 407 that would be rendered outdated by the new rule or otherwise addressed elsewhere by new FINRA rules.

- ▶ The proposed rule eliminates NASD Rule 3050(a)'s requirement that the executing member use reasonable diligence to determine that the execution of the transaction will not adversely affect the interests of the employer member. FINRA believes that this requirement would no longer be needed in light of the approach taken by the proposed rule (*i.e.*, the employer member is responsible for supervising its associated persons' activities).
- ▶ The supervisory requirements of NYSE Rule 407 (*i.e.*, the account review requirements as set forth in NYSE Rule 407(b) and requirements for written procedures as set forth in NYSE Rule 407.11) would be eliminated because these issues are adequately addressed, in combination, by the proposed rule and the new consolidated supervisory rules proposed for inclusion in the Consolidated FINRA Rulebook.¹³

- NYSE Rule 407A (which addresses member reporting of securities accounts to the NYSE) would be deleted in its entirety from the Transitional Rulebook because the proposed rule requires disclosure at the member firm level of the same types of information that Rule 407A requires with respect to the NYSE. FINRA believes it is more appropriate to require member firms to obtain such information from their associated persons and to supervise such accounts for improper trading, rather than requiring such information be sent directly to FINRA.

Request for Comment

FINRA requests comment on proposed FINRA Rule 3210 during the comment period as set forth above. Among other matters that commenters may wish to address, FINRA is particularly interested in the following questions:

- What methodologies do firms currently employ to obtain information pursuant to NASD Rule 3050 or NYSE Rule 407, as applicable? Do firms collect account activity information (confirmations and statements) electronically, in hard copy or both? Should the proposed rule address such information-gathering methodologies and, if so, how?
- What processes and controls do firms currently implement upon receipt of the information required under NASD Rule 3050 or NYSE Rule 407, as applicable?

Endnotes

- 1 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 member firms, 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 member firms, 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).
- 2 For convenience, the Incorporated NYSE Rules are referred to as the NYSE Rules.
- 3 The proposed rule replaces NASD Rule 3050 and corresponding provisions in NYSE Rule 407 (together with its associated Rule Interpretation 407/01). NYSE Rule 407A would also be deleted in its entirety from the Transitional Rulebook.
- 4 FINRA will not edit personal identifying information, such as names or email addresses, from submissions. Persons should submit only information that they wish to make publicly available. See *NASD Notice to Members 03-73* (November 2003) (NASD Announces Online Availability of Comments) for more information.
- 5 Section 19 of the Securities Exchange Act of 1934 (SEA or Exchange Act) permits certain limited types of proposed rule changes to take effect upon filing with the SEC. The SEC has the authority to summarily abrogate these types of rule changes within 60 days of filing. See SEA Section 19 and rules thereunder.
- 6 The terms “person associated with a member” and “associated person of a member” are defined in paragraph (rr) of Article I of the FINRA By-Laws.
- 7 Based on NASD Rule 3050(d) and NYSE Rule 407.13, proposed FINRA Rule 3210.05 defines the terms “other financial institution” and “financial institution other than a member” to include, without limitation, any broker-dealer that is registered pursuant to Section 15(b)(11) of the Exchange Act, domestic or foreign non-member broker-dealer, investment adviser, bank, insurance company, trust company, credit union and investment company.
- 8 FINRA notes that NYSE Rule 407 covers by its terms securities and commodities accounts. In contrast, NASD Rule 3050 generally addresses transactions in securities and the opening of accounts. For purposes of the proposed rule, FINRA does not believe that it is necessary to incorporate express reference to commodities accounts. Further, FINRA believes that specifying “any account in which securities transactions can be effected,” in place of the terms currently used in the NYSE and NASD rules, would set a clarifying standard that accords with the purpose of the proposed rule.

- 9 Generally, NYSE Rule 407 addresses transactions in which the associated person is “directly or indirectly interested” (NYSE Rule 407(a)) or with respect to which the associated person “has any financial interest or the power, directly or indirectly, to make investment decisions” (NYSE Rule 407(b)). In contrast, NASD Rules 3050(b) through (d) generally address accounts and/or transactions in which the associated person has a “financial interest” or over which he or she has “discretionary authority.” For purposes of the proposed rule, FINRA believes that specifying accounts in which the associated person has a “personal financial interest” sets an effective standard that also helps to distinguish transactions subject to this new rule from outside securities activities subject to proposed FINRA Rule 3110(b)(3) (currently, NASD Rule 3040) as set forth in *Regulatory Notice 08-24* (May 2008) (Supervision and Supervisory Controls). In this regard, to limit regulatory duplication, FINRA intends to amend proposed FINRA Rule 3110(b)(3) to exclude generally transactions effected in accounts in which the associated person alone has a personal financial interest (such transactions would be subject to proposed FINRA Rule 3210).
- 10 Based on NYSE Rule 407.12 and NASD Rule 3050(f), proposed FINRA Rule 3210.03 states that the requirement to provide to the employer member duplicate account statements and confirmations would not be applicable to transactions in unit investment trusts and variable contracts or redeemable securities of companies registered under the Investment Company Act, or to accounts that are limited to transactions in such securities, or to Monthly Investment Plan type accounts, unless the employer member requests receipt of such duplicate account statements and confirmations.
- 11 Note that if the account is opened or otherwise established at a financial institution other than a member firm, proposed FINRA Rule 3210.02 provides that, for purposes of proposed FINRA Rule 3210(c), it would be the obligation of the associated person to instruct the institution to provide the duplicate account statements and confirmations to the employer member.
- 12 Currently, NASD Rule 3050(b) requires the executing member to transmit duplicate confirmations and statements upon request by the employer member. FINRA believes that, from the standpoint of sound supervisory practice, providing the duplicates should not be dependent upon receipt of such a request.
- 13 See *Regulatory Notice 08-24* (May 2008) (Supervision and Supervisory Controls).

ATTACHMENT A

Below is the text of proposed FINRA Rule 3210.

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3000. SUPERVISION AND RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS

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3200. RESPONSIBILITIES RELATING TO ASSOCIATED PERSONS

3210. Personal Securities Transactions for or by Associated Persons

(a) No person associated with a member shall, without the prior written consent of the member (“employer member”), open or otherwise establish at a member other than the employer member (“executing member”), or at any other financial institution, any account in which securities transactions can be effected and in which such associated person has a personal financial interest. As a condition to such prior written consent, the employer member must instruct the associated person to have the executing member provide duplicate account statements and confirmations to the employer member.

(b) Any associated person, prior to opening or otherwise establishing an account pursuant to paragraph (a) of this Rule, shall notify in writing the executing member, or other financial institution, of his or her association with the employer member and shall state in such notice that he or she has a personal financial interest in the account.

(c) When an executing member has actual notice that an associated person of an employer member has a personal financial interest in any account opened or otherwise established at the executing member, such executing member shall not execute any securities transactions in that account unless it has obtained the employer member’s prior written consent. In addition, such executing member shall promptly obtain and implement an instruction from the associated person directing that duplicate account statements and confirmations be provided to the employer member.

• • • Supplementary Material: — — — — —

.01 Account Opened Prior to Association With Employer Member. — For the purposes of paragraphs (a) and (b) of this Rule, if the account was opened or otherwise established prior to the person's association with the employer member, the associated person, within fifteen business days of becoming so associated, shall obtain the written consent of the employer member to maintain the account and shall notify in writing the executing member or other financial institution of his or her association with the employer member and personal financial interest. The associated person shall instruct the executing member or other financial institution to provide to the employer member duplicate account statements and confirmations as of the date of his or her association with the employer member.

.02 Account at Financial Institution Other Than a Member. — For the purposes of paragraph (c) of this Rule, with respect to any account opened or otherwise established at a financial institution other than a member, it shall be the obligation of the associated person to instruct the financial institution to provide duplicate account statements and confirmations to the employer member.

.03 Duplicate Account Statements and Confirmations. — The requirement to provide to the employer member duplicate account statements and confirmations shall not be applicable to transactions in unit investment trusts and variable contracts or redeemable securities of companies registered under the Investment Company Act, as amended, or to accounts that are limited to transactions in such securities, or to Monthly Investment Plan type accounts, unless the employer member requests receipt of such duplicate account statements and confirmations.

.04 Failure to Receive Duplicate Account Statements and Confirmations. — If an employer member does not receive the duplicate account statements and confirmations required pursuant to this Rule in a timely manner, the employer member shall revoke its consent to maintain the account, and shall so notify the executing member or other financial institution in writing. The employer member shall promptly obtain records from the executing member that the account was closed.

.05 Other Financial Institution. — For the purposes of this Rule, the terms "other financial institution" and "financial institution other than a member" include, but are not limited to, any broker-dealer that is registered pursuant to Section 15(b)(11) of the Exchange Act, domestic or foreign non-member broker-dealer, investment adviser, bank, insurance company, trust company, credit union and investment company.

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