

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-58905; File No. SR-FINRA-2008-054]

### Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Proposed Rule Change To Adopt FINRA Rule 5280 (Trading Ahead of Research Reports) in the Consolidated FINRA Rulebook

November 6, 2008.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 29, 2008, Financial Industry Regulatory Authority, Inc. ("FINRA") (f/k/a National Association of Securities Dealers, Inc. ("NASD")) filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been substantially prepared by FINRA. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

FINRA is proposing to adopt NASD Interpretive Material 2110-4 (Trading Ahead of Research Reports) as a FINRA rule, subject to certain amendments. The proposed rule change would renumber NASD IM-2110-4 as FINRA Rule 5280 in the consolidated FINRA Rulebook.

The text of the proposed rule change is available at FINRA, on its Web site (<http://www.finra.org>), and at the Commission's Public Reference Room.

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

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

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

##### 1. Purpose

As part of the process of developing the new consolidated rulebook ("Consolidated FINRA Rulebook"),<sup>3</sup> FINRA is proposing to adopt in the Consolidated FINRA Rulebook NASD Interpretive Material ("IM") 2110-4 (Trading Ahead of Research Reports) with certain modifications.

IM-2110-4 states that it is conduct inconsistent with just and equitable principles of trade for a member to establish or adjust an inventory position in an exchange-listed security traded over-the-counter or a derivative of such security in anticipation of the issuance of a research report on that security. The IM further recommends—but does not require—that firms establish policies and procedures to develop and implement effective internal controls to isolate specific information within research and other relevant departments so as to prevent the trading department from utilizing advance knowledge of the issuance of research reports. Those members that choose not to establish such procedures bear the burden to show that changes in inventory positions in advance of research reports were not purposeful.<sup>4</sup>

The proposed rule change would amend the IM in three respects. First, it would extend the application of the IM to cover inventory positions with respect to any security—including debt—or derivative thereof, irrespective of whether the security is exchange-listed. FINRA believes the purpose of the IM—to prevent the manipulation of the supply of a security for the benefit of a firm and to the detriment of investors—applies equally to inventory

positions in non-exchange-listed securities.

Second, the proposed rule change would apply the rule only to circumstances where a member establishes or adjusts its inventory based on *non-public* advance knowledge of the content or timing of a research report in that security. As such, it would not be a violation of the rule for a member to increase or decrease inventory of a security based on publicly available information regarding the likely timing of a research report. By way of example, when a member's trading desk adjusts an inventory position in anticipation of a research report because of a publicly discernible trend that a member's report tends to follow an earnings announcement, the prohibitions of the rule would not be triggered. However, having knowledge of a publicly discernible trend is not a viable alternative basis for the member's trading desk to adjust its inventory position when the trading desk is also the recipient of *non-public* advance knowledge of the content or timing of a research report in that security.

Finally, the proposal would eliminate the option to establish internal controls to manage the flow of information between the research and trading departments and instead mandate that firms establish policies and procedures reasonably designed to restrict or limit the information flow between research department personnel, or other persons with knowledge of the content or timing of a research report, and trading department personnel, so as to prevent trading department personnel from utilizing non-public advance knowledge of the issuance or content of a research report for the benefit of the member or any other person.

FINRA believes that a member should have an affirmative obligation to manage conflicts of interest in its trading of securities. Moreover, this approach is more consistent with existing and proposed rules regarding supervision and the requirements of NASD Rule 2711 and NYSE Rule 472 to eliminate conflicts involving the publication and distribution of research reports.

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

##### 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of section 15A(b)(6) of the Act,<sup>5</sup> which

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

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

<sup>3</sup> The current FINRA rulebook includes, in addition to FINRA Rules, (1) NASD Rules and (2) rules incorporated from NYSE ("Incorporated NYSE Rules") (together, the NASD Rules and Incorporated NYSE Rules are referred to as the "Transitional Rulebook"). While the NASD Rules generally apply to all FINRA members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE ("Dual Members"). For more information about the rulebook consolidation process, see *FINRA Information Notice*, March 12, 2008 (Rulebook Consolidation Process).

<sup>4</sup> Incorporated NYSE Rule Interpretation 401/01 includes aspects similar to IM-2110-4. FINRA deleted that Interpretation as part of an earlier filing to transfer NASD Rules 2110 (Standards of Commercial Honor and Principles of Trade) and 2120 (Use of Manipulative, Deceptive or Other Fraudulent Devices) to the Consolidated FINRA Rulebook, as the conduct addressed in the Interpretation is subsumed by those rules. See Securities Exchange Act Release No. 58643 (September 25, 2008), 73 FR 57174 (October 1, 2008) (Order Approving SR-FINRA-2008-028).

<sup>5</sup> 15 U.S.C. 78o-3(b)(6).

requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will protect the investing public by preventing firms from utilizing non-public advance knowledge of the timing or content of a research report to benefit its own trading to the detriment of its customers. The proposed rule change further would clarify and streamline NASD IM-2110-4 for adoption as a FINRA Rule in the new Consolidated FINRA Rulebook. NASD IM-2110-4 has previously have been found to meet the statutory requirements, and FINRA believes that rule has since proven effective in achieving the statutory mandates.

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

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

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

Written comments were neither solicited nor received.

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

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

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

### **IV. Solicitation of Comments**

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

#### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2008-054 on the subject line.

#### *Paper Comments*

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

All submissions should refer to File Number SR-FINRA-2008-054. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2008-054 and should be submitted on or before December 4, 2008.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>6</sup>

**Florence E. Harmon,**

*Acting Secretary.*

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<sup>6</sup> 17 CFR 200.30-3(a)(12).

### **SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-58898; File No. SR-ISE-2008-81]

#### **Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to its Cancellation Fee**

November 4, 2008.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on October 31, 2008, International Securities Exchange, LLC (the "ISE" or the "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by the Exchange. The ISE filed the proposal pursuant to section 19(b)(3)(A) of the Act<sup>3</sup> and Rule 19b-4(f)(2) thereunder,<sup>4</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The ISE is proposing to amend its Schedule of Fees regarding its cancellation fee. The text of the proposed rule change is available on the Exchange's Web site (<http://www.ise.com>), at the principal office of the Exchange, and at the Commission's Public Reference Room.

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

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

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

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

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A).

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