

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-58660; File No. SR-FINRA-2008-027)

September 26, 2008

Self-Regulatory Organizations: Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change Relating to the Adoption of FINRA Rule 3220 (Influencing or Rewarding Employees of Others) and FINRA Rule 2070 (Transactions Involving FINRA Employees) in the Consolidated FINRA Rulebook

I. Introduction

On July 18, 2008, the Financial Industry Regulatory Authority, Inc. (“FINRA”) (f/k/a National Association of Securities Dealers, Inc. (“NASD”)) filed with the Securities and Exchange Commission (“Commission”) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule relating to the adoption of FINRA Rule 3220 (Influencing or Rewarding Employees of Others) and FINRA Rule 2070 (Transactions Involving FINRA Employees) in the new consolidated FINRA rulebook (“Consolidated FINRA Rulebook”).<sup>3</sup> The proposed rule change was published for comment in the Federal Register on August 11, 2008.<sup>4</sup> The

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

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

<sup>3</sup> The current FINRA rulebook consists of two sets of rules: (1) NASD Rules and (2) rules incorporated from NYSE (“Incorporated NYSE Rules”) (together referred to as the “Transitional Rulebook”). The Incorporated NYSE Rules (hereinafter, “NYSE Rules”) apply only to those members of FINRA that are also members of the NYSE (“Dual Members”). Dual Members also must comply with NASD Rules. For more information about the rulebook consolidation process, see FINRA Information Notice, March 12, 2008 (Rulebook Consolidation Process).

<sup>4</sup> See Securities Exchange Act Release No. 34-58308 (August 5, 2008); 73 FR 46664 (Aug. 11, 2008) (notice).

Commission received one comment letter in response to the proposed rule change.<sup>5</sup> This order approves the proposed rule change.

## II. Description of the Proposed Rule Change

As part of the process of developing the Consolidated FINRA Rulebook, FINRA proposed to transfer without material change NASD Rules 3060 (Influencing or Rewarding Employees of Others) and 3090 (Transactions Involving Association and American Stock Exchange Employees) into the Consolidated FINRA Rulebook and to delete the corresponding provisions in Incorporated NYSE Rules 350, 350.10, 407(a), 407.10 and NYSE Rule Interpretations 350/01 through 350/03. The proposed rule change would renumber NASD Rule 3060 as FINRA Rule 3220 and NASD Rule 3090 as FINRA Rule 2070 in the Consolidated FINRA Rulebook, and would delete NASD Rules 3060 and 3090 in their entirety from the Transitional Rulebook.

### (A) Proposed FINRA Rule 3220

#### (1) Background

NASD Rule 3060 (Influencing or Rewarding Employees of Others) currently states that no member or associated person shall give gifts or gratuities to an agent or employee of another person in excess of \$100 per year where the gift or gratuity is in relation to the business of the employer of the recipient. The rule, which protects against improprieties that may arise when members or their associated persons give gifts or gratuities to employees of a customer, has been in effect in its current form since 1969,

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<sup>5</sup> See letter from Amal Aly, Managing Director and Associate General Counsel, Securities Industry and Financial Markets Association, dated Sept. 2, 2008 (“SIFMA letter”).

with changes only to the dollar amounts, rising from \$25 to \$50 to \$100.<sup>6</sup> The rule requires each member to maintain a separate record of all gifts or gratuities. The rule also contains an express exclusion for payments made pursuant to *bona fide*, written employment contracts.

NYSE Rule 350 (Compensation or Gratuities to Employees of Others) reaches similar conduct in prohibiting, absent prior written consent of the recipient's employer, any member or member organization from giving any gratuity in excess of \$100 per person per year to any principal, officer, or employee of another member or member organization, financial institution, news or financial information media, or non-member broker or dealer in securities, commodities or money instruments.<sup>7</sup> NYSE Rule 350 has specific provisions addressing compensation to operations employees of members (*e.g.*, NYSE Floor personnel). In addition, NYSE Rule 350 requires that records of all such gratuities and compensation be retained for at least three years.

(2) Proposal

FINRA proposed to transfer NASD Rule 3060 into the Consolidated FINRA Rulebook without material change and renumbered as FINRA Rule 3220. One of the advantages of the existing regulatory standard is the clarity of the rule's application – it

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<sup>6</sup> See NASD Notice to Members 93-8 (February 1993) (SEC Approval of Amendment Relating to the Payment of Gratuities or Anything of Value by Members to Others); see also Securities Exchange Act Release No. 21074 (June 20, 1984), 49 FR 26330 (June 27, 1984) (SR-NASD-84-8) (approval order).

<sup>7</sup> In addition, NYSE Rule 350(a)(1) prohibits any member from employing or compensating any person for services rendered except with the prior consent of that person's employer. FINRA proposed to delete this provision, even though it does not pertain to gifts, because a substantively identical provision exists in NYSE Rule 346(b). FINRA intends to review NYSE Rule 346(b) as part of a later phase of the rulebook consolidation process.

prevents gifts in excess of a fixed amount, currently \$100. Both the NASD and NYSE rules have a \$100 limitation on gifts.

FINRA believes that NASD Rule 3060 generally is well understood by members. FINRA recently issued additional guidance on NASD Rule 3060 in Notice to Members 06-69.<sup>8</sup> Among the issues addressed in that Notice was the fact that NASD Rule 3060 does not apply to gifts of *de minimis* value, or to promotional items of nominal value displaying a firm's logo. The Notice stated that NASD Rule 3060 does not prohibit customary Lucite tombstones, plaques or other similar solely decorative items commemorating a business transaction or event. The Notice also stated that gifts should be valued at the higher of cost or market value and tickets should be valued at the higher of cost or face value. In addition, FINRA staff has used its interpretive authority to address unintended consequences of the rule, such as unreasonable limitations on giving a bereavement or sympathy gift.<sup>9</sup>

FINRA proposed to eliminate the provision in NYSE Rule 350 permitting member firms to obtain prior written consent of the recipient's employer for any gift over \$100. FINRA believes that the gift rule should establish a fixed amount and does not see any business need to justify giving gifts in amounts greater than the limits specified in the rule. FINRA also would delete the provisions in NYSE Rule 350 and NYSE Rule Interpretation 350/02 addressing compensation to operations/Floor employees of NYSE

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<sup>8</sup> See NASD Notice to Members 06-69 (December 2006) (Gifts and Gratuities).

<sup>9</sup> See Interpretive Letter dated December 17, 2007 to Amal Aly, SIFMA from Gary L. Goldsholle, FINRA, available at: <<http://www.finra.org/RulesRegulation/PublicationsGuidance/InterpretiveLetters/ConductRules/P037695>>.

as they are not relevant for FINRA.<sup>10</sup> For similar reasons, provisions in NYSE Rule 350.10 pertaining to employment of or gratuities to personnel working the Floor of other exchanges would be deleted.<sup>11</sup> Finally, FINRA would eliminate the provisions of NYSE Rule 350 relating to record retention, as NASD Rule 3060(c) addresses the same issue. FINRA proposed to eliminate NYSE Rule Interpretation 350/01, and provisions in NYSE Rule 350.10 pertaining to gifts among close relatives, because the concepts contained in both are adequately addressed by proposed FINRA Rule 3220 and existing guidance. Lastly, FINRA would eliminate NYSE Rule Interpretation 350/03 because FINRA has proposed a separate rule that addresses business entertainment.<sup>12</sup> Any guidance provided under NASD Rule 3060, including, without limitation, notices to members and interpretation letters, also would apply to the proposed FINRA Rule 3220.<sup>13</sup> The Commission notes three interpretative letters previously issued with respect to NASD

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<sup>10</sup> NYSE Rule Interpretation 350/02 would be deleted in its entirety. Note that NYSE Rule 350 also contains provisions that address gifts and gratuities to employees of the NYSE. These provisions are addressed in connection with FINRA's proposal to adopt FINRA Rule 2070. See Section (B) under Item II.A.1. FINRA's proposals with respect to FINRA Rules 3220 and 2070 would, in combination, delete NYSE Rule 350 in its entirety.

<sup>11</sup> NYSE Rule 350.10 also contains provisions that address employment or compensation of NYSE employees by members or member organizations. These provisions are addressed in connection with FINRA's proposal to adopt FINRA Rule 2070. See Section (B) under Item II.A.1. Because Proposed FINRA Rules 3220 and 2070 would address the substance of NYSE Rule 350.10, FINRA proposed to delete NYSE Rule 350.10 in its entirety.

<sup>12</sup> See Securities Exchange Act Release No. 55765 (May 15, 2007), 72 FR 28743 (May 22, 2007) (notice) see also Amendment No. 3 to File No. SR-NASD-2006-044 (January 2, 2008).

<sup>13</sup> Telephone conference among Gary Goldsholle and Adam Arkel, FINRA, and Haimera Workie, Branch Chief, Alicia Goldin, Special Counsel, Sharon Lawson, Senior Special Counsel and Steve Kuan, Special Counsel, Commission, on September 11, 2008.

Rule 3060.<sup>14</sup> The interpretative letters include FINRA's rule on members providing business entertainment.<sup>15</sup>

(B) Proposed FINRA Rule 2070

(1) Background

Both NASD and NYSE rules address conflicts of interest involving FINRA and NYSE employees.

NASD Rule 3090 addresses this issue in three ways. First, NASD Rule 3090(a) requires a member, when it has actual notice that an NASD employee has a financial interest or controls trading in an account, to promptly obtain and implement an instruction from the employee directing that duplicate account statements be provided by the member to NASD. Second, NASD Rule 3090(b) prohibits a member from making any loan of money or securities to an NASD employee. This prohibition does not apply to loans made in the context of disclosed, routine banking and brokerage agreements, or loans that are clearly motivated by a personal or family relationship. Third, NASD Rule 3090(c) prohibits any member from directly or indirectly giving, or permitting to be given, anything of more than nominal value to any NASD employee who has responsibility for a regulatory matter involving the member. This applies regardless of the \$100 per individual per year limitation set forth in NASD Rule 3060(a). The term “regulatory matter” is defined to include, without limitation, examinations, disciplinary

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<sup>14</sup> These interpretative letters are currently available at FINRA's web site at <http://www.finra.org/Industry/Regulation/Guidance/InterpretiveLetters/ConductRules/index.htm>.

<sup>15</sup> See, e.g., letter to Henry H. Hopkins and Sarah McCafferty, T. Rowe Price Investment Services, Inc., dated June 24, 1999.

proceedings, membership applications, listing applications, delisting proceedings, and dispute-resolution proceedings that involve the member.

The NYSE rules governing conflicts of interest involving NYSE employees differ from the NASD approach in two ways. First, rather than applying the duplicate statement approach to NYSE employees (which applies to NASD employees under NASD Rule 3090(a)), NYSE Rule 407(a) prohibits a member or member organization, without the prior written consent of the NYSE, from opening a securities or commodities account or executing any transaction in which an employee of the NYSE is directly or indirectly interested.<sup>16</sup> NYSE Rule 401.10 states that an employee of the NYSE or any of its affiliated companies who wishes to open a securities or commodities account should apply for permission from the NYSE's Ethics Officer. Second, the NYSE Rules differ from the nominal value approach set forth in NASD Rule 3090(c) by instead setting procedures for outside compensation and placing a dollar limit on gifts. Specifically, with respect to outside compensation, NYSE Rule 350(a)(1) prohibits any member, allied member, member organization or employee thereof from employing or compensating any person for services rendered without the prior consent of the person's employer (*i.e.*, the NYSE with respect to NYSE employees).<sup>17</sup> With respect to gifts, NYSE Rule 350(a)(2)

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<sup>16</sup> NYSE Rule 407(a) requires duplicate confirmations and account statements with respect to accounts or transactions of members, allied members and employees associated with another member or member organization.

<sup>17</sup> NYSE Rule 350.10 provides that requests for NYSE consent under Rule 350(a)(1) should be sent to the NYSE's Human Resources Department at least 10 days in advance of the proposed date of employment. NYSE Rule 350.10 states that approval to employ an NYSE employee outside the hours of regular employment by the NYSE will be limited to employment of a routine or clerical nature. NYSE Rule 350.10 further states that when the NYSE has granted permission for part-time employment of a NYSE employee, no approval is required for a subsequent

prohibits giving any gift or gratuity in excess of \$50 per person per year to any principal, officer, or employee of the NYSE or its subsidiaries without the prior written consent of the NYSE. This rule is written without regard to whether the NYSE employee has responsibility for regulatory matters affecting the member.

(2) Proposal

FINRA proposed to transfer NASD Rule 3090 into the Consolidated FINRA Rulebook without material change,<sup>18</sup> renumbered as FINRA Rule 2070 and that the corresponding provisions in NYSE Rules 350(a)(1), 350(a)(2), 350.10, 407(a) and 407.10 be eliminated.<sup>19</sup> Rather than requiring the member to obtain FINRA's consent to open a securities or commodities account or execute a trade (as set forth under NYSE Rules 407(a) and 407.10), FINRA believes that it is sufficient, as set forth under NASD Rule 3090(a), to continue to require the member to obtain and implement an instruction from the FINRA employee directing the member to provide duplicate statements to FINRA. The proposed rule change would, as set forth in NASD Rule 3090(b), continue to prohibit members from making any loan of money or securities to a FINRA employee, subject to the exceptions set forth in that rule. Lastly, the proposed rule change would, as set forth in NASD Rule 3090(c), continue to prohibit members from directly or indirectly giving, or permitting to be given, anything above nominal value to any FINRA employee who

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gratuity or bonus to such person provided it is in proportion to gratuities given to full-time employees of the employing organization.

<sup>18</sup> The proposal included stylistic edits to NASD Rule 3090 for purposes of clarity and readability.

<sup>19</sup> With respect to NYSE Rule 407(a), the only change to the rule at this stage in the rulebook consolidation would be to delete language pertaining to employees of the NYSE. See Exhibit 5. NYSE Rule 407.10 would be deleted in its entirety. With respect to NYSE Rules 350(a)(1), 350(a)(2) and 350.10, see supra notes 10 and 11.



has responsibility for a “regulatory matter” involving the member. FINRA does not believe that its employees should be permitted to receive gifts of up to \$50 per year when such employees have responsibility for a regulatory matter. In addition, FINRA proposed not to adopt the \$50 limit in NYSE Rule 350(a)(2) for gifts to all other employees to maintain consistency with the FINRA Code of Conduct, which, like NASD Rule 3060(a) (and proposed FINRA Rule 3220(a)), establishes a \$100 limit. Rule 3090(c) need not be amended to address the employment and compensation issues as to NYSE employees in NYSE Rules 350(a)(1) and 350.10 because the FINRA Code of Conduct addresses these issues through its provisions on Outside Activities or Employment.

FINRA proposed to delete listing and delisting proceedings as potential “regulatory matters” under NASD Rule 3090(c) in light of FINRA’s separation from NASDAQ and The American Stock Exchange.

### III. Comment Letters

The Commission received one comment letter on the proposal<sup>20</sup> and a response to comments from FINRA.<sup>21</sup> In its comment letter, SIFMA supported FINRA’s effort to consolidate its two rulebooks.<sup>22</sup> However, SIFMA suggested that FINRA should amend the proposed rule change with respect to NASD Rule 3060 to incorporate a principles-based approach to gifts and gratuities.<sup>23</sup> SIFMA said that FINRA should permit firms to establish their own gifts and gratuities policies and limits rather than retain the limits set

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<sup>20</sup> See supra, footnote 5.

<sup>21</sup> See letter from Gary L. Goldsholle, Vice President and Associate General Counsel, FINRA Regulatory Group, dated September 11, 2008.

<sup>22</sup> See SIFMA letter.

<sup>23</sup> Id.

forth in the rule.<sup>24</sup> SIFMA also supports the inclusion of a safe harbor in new Rule 3220, under which a FINRA member firm would be deemed to be in compliance with new Rule 3220, if the aggregate annual amount of gifts and gratuities to any one person did not exceed a de minimis amount, such as \$250.<sup>25</sup>

FINRA responded to the request by SIFMA for a principles-based approach to gifts and gratuities by stating that FINRA had given a great deal of consideration to this approach, but had determined to maintain the existing standards, which offer predictability and clarity.<sup>26</sup> FINRA also noted that it does not believe that it is appropriate at this time to increase the limit for gifts and gratuities to \$250 from \$100.<sup>27</sup>

#### IV. Discussion and Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act, and the rules and regulations thereunder that are applicable to a national securities association.<sup>28</sup> In particular, the Commission believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>29</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The Commission believes that, as part of the FINRA rulebook consolidation process, the

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<sup>24</sup> Id.

<sup>25</sup> Id.

<sup>26</sup> See supra, footnote 21.

<sup>27</sup> Id.

<sup>28</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition and capital formation. See 15 U.S.C. 78c(f).

<sup>29</sup> 15 U.S.C. 78o-3(b)(6).

proposed rule change would streamline and reorganize existing rules that govern influencing or rewarding the employees of others and transactions involving FINRA employees. Further, the proposed rule change would provide greater regulatory clarity with respect to these issues.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>30</sup> that the proposed rule change (SR-FINRA-2008-027) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>31</sup>

Florence E. Harmon  
Acting Secretary

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<sup>30</sup> 15 U.S.C. 78s(b)(2).

<sup>31</sup> 17 CFR 200.30-3(a)(12).