Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act[14] and Rule 19b–4(f)(6) thereunder.[15]

A proposed rule change filed under 19b–4(f)(6) normally may not become operative prior to 30 days after the date of filing.[16] However, Rule 19b–4(f)(6)(iii)[17] permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. FINRA has requested that the Commission waive the 30-day operative delay. The Commission notes that FINRA's proposal is substantially similar to the rules of the Options Exchanges and does not raise any new substantive issues.[18] The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest because such waiver will allow FINRA to harmonize its rules with the rules of the Options Exchanges without undue delay. The Commission hereby grants FINRA's request and designates the proposal operative upon filing.[19]

At any time within 60 days of the filing of such proposed rule change the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors or otherwise in furtherance of the purposes of the Act.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposal 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*. Please include File No. SR–FINRA–2009–032 on the subject line.

Paper Comments

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

All submissions should refer to File No. SR–FINRA–2009–032. 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 changes 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 No. SR–FINRA–2009–032 and should be submitted on or before June 18, 2009.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[20]

Florence E. Harmon,

Deputy Secretary.

[FR Doc. E9–12311 Filed 5–27–09; 8:45 am]

BILLING CODE 8010–01–P

[14] 15 U.S.C. 78s(b)(3)(A).

[15] 17 CFR 240.19b–4(f)(6).

[16] 17 CFR 240.19b–4(f)(6)(iii). In addition, Rule 19b–4(f)(6)(iii) requires that a self-regulatory organization submit to the Commission written notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. FINRA has satisfied this notice requirement.

[17] *Id.*

[18] *See supra* note 5 and 11.

[19] For the purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[20] 17 CFR 200.30–3(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–59955; File No. SR–FINRA–2009–012]

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change, as Modified by Amendment No. 1, To Implement an Interim Pilot Program With Respect to Margin Requirements for Certain Transactions in Credit Default Swaps

May 22, 2009.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4 thereunder,[2] notice is hereby given that on March 11, 2009, 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 and II below, which Items substantially have been prepared by FINRA. On May 19, 2009, FINRA submitted Amendment No. 1 to the proposed rule change. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons and is simultaneously approving the proposed rule change as amended on an accelerated basis to establish an interim pilot program.

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

FINRA is proposing to adopt FINRA Rule 4240 (Margin Requirements for Credit Default Swaps). The proposed rule would implement an interim pilot program (the ''Interim Pilot Program'') with respect to margin requirements for transactions in credit default swaps (''CDS'') executed by a member (regardless of the type of account in which the transaction is booked), including those in which the offsetting matching hedging transactions (''matching transactions'') are effected by the member in CDS contracts that are cleared through the central counterparty clearing services of the Chicago Mercantile Exchange (the ''CME''). The proposed rule would expire on September 25, 2009.

The text of the proposed rule change is available on FINRA's Web site at *http://www.finra.org,* at the principal office of FINRA and at the Commission's Public Reference Room.

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

In addition, the text of the proposed rule change is set forth below. New language is in italics.

* * * * *

4000. FINANCIAL AND OPERATIONAL RULES

* * * * *

4200. MARGIN

* * * * *

4240. Margin Requirements for Credit Default Swaps

(a) Effective Period of Interim Pilot Program

This Rule establishes an interim pilot program (''Interim Pilot Program'') with respect to margin requirements for any transactions in credit default swaps executed by a member (regardless of the type of account in which the transaction is booked), including those in which the offsetting matching hedging transactions (''matching transactions'') are effected by the member in contracts that are cleared through the central counterparty clearing services of the Chicago Mercantile Exchange (''CME''). The Interim Pilot Program shall automatically expire on September 25, 2009. For purposes of this Rule, the term ''credit default swap'' (''CDS'') shall mean any ''eligible credit default swap'' as defined in Securities Act Rule 239T(d), as well as any other CDS that would otherwise meet such definition but for being subject to individual negotiation, and the term ''transaction'' shall include any ongoing CDS position.

(b) Central Counterparty Clearing Arrangements

Any member, prior to establishing any clearing arrangement with respect to CDS transactions that makes use of any central counterparty clearing services provided by any clearing agency, pursuant to Securities Act Rule 239T(a)(1), must notify FINRA in advance in writing, in such manner as may be specified by FINRA in a Regulatory Notice.

(c) Margin Requirements

(1) CDS Cleared on the Chicago Mercantile Exchange

Members shall require as a minimum for computing customer or broker-dealer margin, with respect to any customer or broker-dealer transaction in CDS with a member in which the member executes a matching transaction that makes use of the central counterparty clearing facilities of the CME (''CME matching customer-side transaction''), the applicable margin pursuant to CME rules (sometimes referred to in such rules as a ''performance bond'') regardless of the type of account in which the transaction in CDS is booked. Members shall, based on the risk monitoring procedures and guidelines set forth in paragraph (d) of this Rule, determine whether the applicable CME requirements are adequate with respect to their customer and broker-dealer accounts and the positions in those accounts and, where appropriate, increase such margin in excess of such minimum margin. For this purpose, members are permitted to use the margin requirements set forth in Supplementary Material .01 of this Rule.

The aggregate amount of margin the member collects from customers and broker-dealers for transactions in CDS must equal or exceed the aggregate amount of margin the member is required to post at CME with respect to those customer and broker-dealer transactions.

CME matching customer-side transactions are not subject to the provisions of paragraph (c)(2) of this Rule.

(2) CDS That Are Cleared on Central Counterparty Clearing Facilities Other Than the CME or That Settle Over-the-Counter (''OTC'')

Members shall require, with respect to any transaction in CDS that makes use of central counterparty clearing facilities other than the CME or that settle OTC, the applicable minimum margin as set forth in Supplementary Material .01 of this Rule regardless of the type of account in which the transaction in CDS is booked. However, members shall, based on the risk monitoring procedures and guidelines set forth in paragraph (d) of this Rule, determine whether such margin is adequate with respect to their customer and broker-dealer accounts and, where appropriate, increase such requirements.

(d) Risk Monitoring Procedures and Guidelines

Members shall monitor the risk of any customer or broker-dealer accounts with exposure to CDS and shall maintain a comprehensive written risk analysis methodology for assessing the potential risk to the member's capital over a specified range of possible market movements over a specified time period. For purposes of this Rule, members must employ the risk monitoring procedures and guidelines set forth in paragraphs (d)(1) through (8) of this Rule. The member must review, in accordance with the member's written procedures, at reasonable periodic intervals, the member's credit extension activities for consistency with the risk monitoring procedures and guidelines set forth in this Rule, and must determine whether the data necessary to apply the risk monitoring procedures and guidelines is accessible on a timely basis and information systems are available to adequately capture, monitor, analyze and report relevant data, including:

(1) obtaining and reviewing the required account documentation and financial information necessary for assessing the amount of credit to be extended to customers and broker-dealers;

(2) assessing the determination, review and approval of credit limits to each customer and broker-dealer, and across all customers and broker-dealers, engaging in CDS transactions;

(3) monitoring credit risk exposure to the member from CDS, including the type, scope and frequency of reporting to senior management;

(4) the use of stress testing of accounts containing CDS contracts in order to monitor market risk exposure from individual accounts and in the aggregate;

(5) managing the impact of credit extended related to CDS contracts on the member's overall risk exposure;

(6) determining the need to collect additional margin from a particular customer or broker-dealer, including whether that determination was based upon the creditworthiness of the customer or broker-dealer and/or the risk of the specific contracts;

(7) monitoring the credit exposure resulting from concentrated positions within both individual accounts and across all accounts containing CDS contracts; and

(8) maintaining sufficient margin in each customer and broker-dealer account to protect against the default of the largest individual exposure in the account as measured by computing the largest maximum possible loss.

(e) Concentrations

Where the maximum current and potential exposure with respect to the largest single name CDS across all accounts exceeds the member's tentative net capital, the member must take a capital charge equal to the aggregate margin requirement for such accounts on the positions in such single name CDS in accordance with the tables set forth in Supplementary Material .01 of this Rule. This capital charge may be reduced by the amount of excess margin held in all customer and broker-dealer accounts.

** * * Supplementary Material:*

.01 Margin Requirements for CDS. The following customer and broker-dealer margin requirements shall apply, as appropriate, pursuant to paragraph (c) of this Rule.

(a) Customer and Broker-Dealer Accounts That Are Short a CDS

The following table shall be used to determine the margin that a member must collect from a customer or broker-dealer that is short a single name debt security CDS contract (sold protection). The margin is to be collected based upon the basis point spread over LIBOR of the CDS contract as well as the maturity of that contract as a percentage of the notional amount, shall be as follows:

Basis point spread	Length of time to maturity of CDS contract (in percent)			
	1 year	3 years	5 years	7 years & longer
0–100	1	2	4	7
100–300	2	5	7	10
300–500	5	10	15	20
500–700	10	15	20	25
700 and above	15	20	25	30

For those CDS contracts where the underlying obligation is a debt index, rather than a single name bond, the margin requirement as a percentage of the notional amount shall be as follows:

Index	Length of time to maturity of CDS contract (in percent)				
	1 year	3 years	5 years	7 years	10 years
CDX.IG	1	1	2	4	5
CDX.HY	3	5	10	12	15
CDX.HVOL	2	3	4	5	7

(b) Accounts That Are Long a CDS

For customer or broker-dealer accounts that are long the CDS contracts (purchased protection), the margin to be collected shall be 50% of the above amounts.

(c) Accounts That Maintain Both Long and Short CDS

In instances where the customer or broker-dealer maintains both long and short CDS, the member may elect to collect 50% of the above margin requirements on the greater of the long or short position within the same Bloomberg CDS sector, provided those long and short positions are in the same spread and maturity bucket.

If a customer or broker-dealer is long the bond and long a CDS contract on the same underlying obligor, margin needs to be collected only on the long bond position, provided that bond can be delivered against the long CDS contract, as prescribed pursuant to applicable FINRA margin rules.

In instances where the customer or broker-dealer is short the bond and short the CDS on the same underlying obligor, margin need only be collected on the short bond, as prescribed pursuant to applicable FINRA margin rules.

* * * * *

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

FINRA is proposing to adopt FINRA Rule 4240 (Margin Requirements for Credit Default Swaps). The proposed rule would implement an Interim Pilot Program with respect to margin requirements for transactions in CDS executed by a member (regardless of the type of account in which the transaction is booked), including those in which matching transactions are effected by the member in CDS contracts that are cleared through the central counterparty clearing services of the CME. The proposed rule would expire on September 25, 2009.

(A). Background

On March 13, 2009, the Commission issued an Order granting temporary exemptions under the Exchange Act in response to a request by CME and Citadel Investment Group, LLC with respect to their proposal for CME to provide clearance and settlement services as a central counterparty for certain transactions in CDS.[3] The Commission issued similar Orders to LCH.Clearnet Ltd[4] and ICE U.S. Trust LLC.[5] The Commission also recently enacted interim final temporary rules providing enumerated exemptions under the federal securities laws for certain CDS to facilitate the operation of one or more central clearing counterparties in such CDS.[6] Finally,

[3] *See* Securities Exchange Act Release No. 59578 (Mar. 13, 2009), 74 FR 11781 (Mar. 19, 2009).

[4] *See* Securities Exchange Act Release No. 59164 (Dec. 24, 2008), 74 FR 139 (Jan. 2, 2009).

[5] *See* Securities Exchange Act Release No. 59527 (Mar. 6, 2009), 74 FR 10791 (Mar. 12, 2009).

[6] *See* Securities Act Release No. 8999 (Jan. 14, 2009), 74 FR 3967 (Jan. 22, 2009) (Temporary Exemptions for Eligible Credit Default Swaps To Facilitate Operation of Central Counterparties To Clear and Settle Credit Default Swaps). Generally, as noted by the Commission, a CDS is a bilateral contract between two parties, known as counterparties. The value of this contract is based on underlying obligations of a single entity or on

the Commission has provided temporary exemptions in connection with Sections 5 and 6 of the Exchange Act for transactions in non-excluded CDS [7] (these Commission actions are hereinafter referred to collectively as the ''Commission's CDS Relief''). The Commission noted that these measures were intended to address concerns arising from systemic risk posed by CDS, including, among others, risks to the financial system arising from the lack of a central clearing counterparty to clear and settle CDS.[8]

Historically, in the absence of a central clearing counterparty, CDS transactions entered into by U.S. investment banks have not been booked in the member, but rather in the affiliated entities. In light of the rapid growth of the CDS market, and the potential inability of parties to meet their obligations as counterparties, the lack of a central clearing counterparty poses risks not only to the two parties to a CDS transaction, but also to the financial system overall because of the resulting chain of significant economic loss when one or more parties default on their obligations under a CDS transaction.

As discussed above, the Commission has issued exemptive Orders to allow three entities to act as CDS central clearing counterparties. Of these, the CME has requested that FINRA adopt customer margin rules for CDS and suggested a specific customer margin methodology that could be employed.[9] FINRA performed an analysis of the margin methodology suggested by CME, as well as the alternative methodology for CDS [10] prior to proposing Rule 4240. FINRA believes it is appropriate to adopt the proposed customer margin rule for CDS transactions during a limited pilot period for the reasons described below; however, FINRA represents that it will consider proposals it receives from other CDS central clearing counterparties to amend its customer margin rules for CDS and, if appropriate, will propose changes to its customer margin rules for CDS.[11]

Accordingly, FINRA proposes to adopt Proposed FINRA Rule 4240, which would impose margin rules for certain CDS transactions. The Interim Pilot Program is intended to be coterminous with the Commission's CDS Relief and would expire on September 25, 2009.

FINRA requests comment on the proposed rule during the period of the Interim Pilot Program. Among other matters that commenters may wish to address, FINRA is particularly interested in the following questions:

1. Since historically CDS transactions have not been undertaken in broker-dealers and therefore have not exposed broker-dealers to the risks of such transactions, is the advent of broker-dealer participation in these transactions, which entails greater individual risks to broker-dealers but which fosters less systemic risk because of the existence of a central clearing party for the matching transaction, a correct balancing of risks as a matter of public policy?

2. Do commenters believe that different or amended margin provisions would be superior to those set forth in the proposed rule?

(B). Proposal

(1) Scope of the Proposed Rule

Proposed FINRA Rule 4240(a) provides that the Interim Pilot Program would apply to margin requirements for any transactions in CDS executed by a member (regardless of the type of account in which the transaction is booked), including those in which the matching transactions are effected by the member in contracts that are cleared through the central clearing counterparty clearing services of the CME. FINRA notes that matching transactions that are cleared through the CME as the central clearing counterparty would be subject to margin requirements pursuant to CME rules (sometimes referred to in such rules as ''performance bond''). Accordingly, with respect to these matching transactions, the proposed rule is intended to apply to the side of the CDS transaction—executed between a member and a customer or other broker-dealer [12]—that is *not* cleared through the CME.[13]

Proposed FINRA Rule 4240(a) would define the term ''CDS'' for purposes of the rule. Specifically, CDS would include any ''eligible credit default swap'' as defined in Securities Act Rule 239T(d),[14] as well as any other CDS that would otherwise meet such definition but for being subject to individual negotiation.[15] In addition, the proposed rule provides that, for purposes of the rule, the term ''transaction'' includes any ongoing CDS position.

Proposed FINRA Rule 4240(a) provides that the Interim Pilot Program would automatically expire on September 25, 2009.

(2) Central Counterparty Clearing Arrangements

Proposed FINRA Rule 4240(b) would provide that any member, prior to establishing any clearing arrangement with respect to CDS transactions that makes use of any central counterparty clearing services provided by any clearing agency, pursuant to Securities Act Rule 239T(a)(1),[16] must notify FINRA in advance in writing, in such manner as may be specified by FINRA in a *Regulatory Notice.*

(3) Margin Requirements: CDS Cleared on the CME

Proposed FINRA Rule 4240(c)(1) provides that a member, as a minimum for computing customer or broker-dealer margin, with respect to any customer or broker-dealer transaction in CDS with a member in which the member executes a CME matching customer-side transaction, must require the applicable margin pursuant to CME rules regardless of the type of account in which the transaction in CDS is booked. The proposed rule would require that members must, based on the risk monitoring procedures and guidelines set forth in paragraph (d) of the proposed rule,[17] determine whether the applicable CME requirements are adequate with respect to their customer and broker-dealer accounts and the positions in those accounts and, where appropriate, increase such margin in excess of the minimum margin. For this purpose, the proposed rule would

a particular security or other debt obligation, or an index of several such entities, securities, or obligations. The obligation of a seller to make payments under a CDS contract is triggered by a default or other credit event as to such entity or entities or such security or securities.

[7] *See* Securities Exchange Act Release No. 59165 (Dec. 24, 2008), 74 FR 133 (Jan. 2, 2009).

[8] *See supra,* notes 3, 4, 5, 6, and 7.

[9] The methodology CME proposed was amended based on FINRA's analysis. FINRA's proposed rule sets forth additional requirements. *See* Proposed FINRA Rule 4240(c)(1).

[10] *See* Proposed FINRA Rule 4240(c)(2).

[11] Based on communications on or about April 22, 2009 between Bonnie Gauch of the Commission's Division of Trading and Markets and Grace Vogel of FINRA.

[12] NASD Rule 0120(g) states that the term ''customer'' shall not include a broker or dealer. For purposes of the proposed rule, the terms ''customer or broker-dealer'' and ''customer and broker-dealer'' are intended to include any party with which a member executes a CDS transaction.

[13] Under Proposed FINRA Rule 4240(c)(1), such transactions are defined as ''CME matching customer-side transactions.'' *See* Section (B)(3) under this Item. Under Proposed FINRA Rule 4240(c)(1), the term ''CME matching customer-side transaction'' would include any party, including a broker-dealer.

[14] 17 CFR 230.239T(d).

[15] FINRA notes that Rule 239T(d) excludes contracts that are ''subject to individual negotiation.'' The proposed FINRA rule would reach CDS contracts, subject to the other criteria set forth in Rule 239T(d), without regard to whether they are individually negotiated.

[16] 17 CFR 230.239T(a)(1).

[17] *See* Proposed FINRA Rule 4240(d).

permit members to use the margin requirements set forth in the proposed rule's Supplementary Material.[18]

It is FINRA's understanding that, after calculating margin on an account-specific basis, CME performs stress tests to assess concentration risk across a member's customer and house portfolios.[19] Further, CME may require that a member post additional margin based on the results of those concentration risk stress tests. Accordingly, Proposed FINRA Rule 4240(c)(1) would require that the aggregate amount of margin the member collects from customers and broker-dealers for transactions in CDS must equal or exceed the aggregate amount of margin the member is required to post at CME with respect to those customer and broker-dealer transactions.

CME matching customer-side transactions, being subject to the margin guidelines set forth in Proposed FINRA Rule 4240(c)(1), are not subject to the margin guidelines as set forth in paragraph (c)(2) of the proposed rule. However, members are encouraged to apply higher margin requirements where appropriate.

(4) Margin Requirements: CDS That Are Cleared on Central Counterparty Clearing Facilities Other Than the CME or That Settle Over-the-Counter (''OTC'')

Proposed FINRA Rule 4240(c)(2) would provide that a member, with respect to any transaction in CDS that makes use of central counterparty clearing facilities other than the CME or that settle OTC, must require the applicable minimum margin as set forth in the proposed rule's Supplementary Material regardless of the type of account in which the transaction in CDS is booked.[20] However, the proposed rule provides that a member must, based on the risk monitoring procedures and guidelines set forth in paragraph (d) of the proposed rule, determine whether such margin is adequate with respect to their customer and broker-dealer accounts and, where appropriate, increase the requirements.

(5) Risk Monitoring Procedures and Guidelines

Proposed FINRA Rule 4240(d) provides that members must monitor the risk of any customer or broker-dealer accounts with exposure to CDS and must maintain a comprehensive written risk analysis methodology for assessing the potential risk to the member's capital over a specified range of possible market movements over a specified time period. The proposed rule would require that members must employ the risk monitoring procedures and guidelines set forth in Proposed FINRA Rule 4240(d)(1) through (8).[21] Further, the rule would require the member to review, in accordance with the member's written procedures, at reasonable periodic intervals, the member's credit extension activities for consistency with the risk monitoring procedures and guidelines set forth in the rule, and to determine whether the data necessary to apply the risk monitoring procedures and guidelines is accessible on a timely basis and information systems are available to adequately capture, monitor, analyze and report relevant data (*i.e.*, the data relevant for purposes of the risk monitoring procedures and guidelines set forth in Proposed FINRA Rule 4240(d)(1) through (8)).

(6) Concentrations

Proposed FINRA Rule 4240(e) would require that, where the maximum current and potential exposure with respect to the largest single name CDS across all accounts exceeds the member's tentative net capital, the member must take a capital charge equal to the aggregate margin requirement for such accounts on the positions in such single name CDS in accordance with the tables set forth in the proposed rule's Supplementary Material.[22] This additional requirement for concentrated positions reflects FINRA's concern for the possibility of a sudden default in the largest single name CDS across all accounts in respect of which a member has current or potential exposure. However, the proposed rule would allow a member to reduce this capital charge by the amount of the excess margin held in all customer and broker-dealer accounts.

(7) Proposed FINRA Rule 4240.01

Proposed FINRA Rule 4240.01, a Supplementary Material, sets forth the customer and broker-dealer margin requirements that would apply with respect to CDS, as appropriate, pursuant to paragraph (c) of the proposed rule. The proposed rule addresses customer and broker-dealer accounts that are short a CDS, accounts that are long a CDS and accounts that maintain both long and short CDS. Paragraph (c) of the Supplementary Material provides, with respect to accounts that maintain both long and short CDS, that if a customer or broker-dealer is long the bond and long a CDS contract on the same underlying obligor, margin would need to be collected only on the long bond position, provided that bond can be delivered against the long CDS contract, as prescribed pursuant to applicable FINRA margin rules.[23] In instances where the customer or broker-dealer is short the bond and short the CDS on the same underlying obligor, margin need only be collected on the short bond, again as prescribed pursuant to applicable FINRA margin rules.[24] FINRA notes that, for purposes of the proposed rule, the term ''applicable FINRA margin rules'' refers to requirements pursuant to NASD Rule 2520 or Incorporated NYSE Rule 431, as applicable to the member.[25] FINRA plans to address NASD Rule 2520 and Incorporated NYSE Rule 431 later as part of FINRA's rulebook consolidation process, and, accordingly, will amend Proposed FINRA Rule 4240.01(c) as appropriate to refer to the new, consolidated FINRA margin rule.[26]

FINRA will announce the effective date of the proposed rule change in a *Regulatory Notice* to be published no later than 60 days following Commission approval, but FINRA does

[18] *See* Proposed FINRA Rule 4240.01.

[19] *See* Letter from Adam Cooper, Senior Managing Director and General Counsel, Citadel Investment Group, L.L.C., and Ann K. Shulman, Managing Director and Deputy General Counsel, Chicago Merchantile Exchange Inc., to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated March 12, 2009 (available at *http://www.sec.gov/rules/exorders/2009/cme-citadel-exreq.pdf*). Letter from Lisa A. Dunsky, Director & Associate General Counsel, CME Group, to David Stawick, Secretary, Commodity Futures Trading Commission, dated December 19, 2008, (available at: *http://www.cftc.gov*).

[20] *See* Proposed FINRA Rule 4240.01.

[21] *See* Proposed FINRA Rule 4240(d)(1) through (8).

[22] *See* Proposed FINRA Rule 4240.01.

[23] As originally proposed, the rule change would have stated, ''If a customer or broker-dealer is long the bond and long a CDS contract on the same underlying obligor, margin needs to be collected only on the long bond position, provided that bond can be delivered against the *short* CDS contract, as prescribed pursuant to applicable FINRA margin rules.'' Amendment No. 1 corrected this sentence by changing the word ''short'' directly preceding the second ''CDS'' to ''long.''

[24] As originally proposed, the rule change would have stated, ''In instances where the customer or broker-dealer is short the bond and short the CDS, margin need only be collected on the short bond, as prescribed pursuant to applicable FINRA margin rules.'' Amendment No. 1 clarified this sentence by adding the phrase ''on the same underlying obligor'' directly following the word ''CDS.''

[25] The current FINRA rulebook consists of: (1) FINRA Rules; (2) NASD Rules; and (3) rules incorporated from NYSE (''Incorporated NYSE Rules''). While the NASD Rules generally apply to all FINRA members, the Incorporated NYSE Rules apply only to those members of FINRA that are also members of the NYSE (''Dual Members''). The FINRA Rules apply to all FINRA members, unless such rules have a more limited application by their terms.

[26] For more information about the rulebook consolidation process, *see* FINRA *Information Notice*, March 12, 2008 (Rulebook Consolidation Process).

intend to issue such *Regulatory Notice* as soon as practicable in the event of SEC approval of the proposed rule change given the limited time period of the proposed Interim Pilot Program.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,[27] which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change would further the purposes of the Act because, consistent with goals set forth by the Commission when it provided the Commission's CDS Relief with respect to the operation of central counterparties to clear and settle CDS, the margin requirements set forth by the proposed rule change will help to stabilize the financial markets.

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. Commission's Findings and Order Granting Accelerated Approval of a Proposed Rule Change

Pursuant to Section 19(b)(2) of the Act,[28] the Commission may not approve any proposed rule change, or amendment thereto, prior to the 30th day after the date of publication of notice of the filing thereof, unless the Commission finds good cause for so doing and publishes its reasons for so finding. FINRA also has requested that the Commission find good cause for approving the proposed rule change prior to the 30th day after publication in the **Federal Register**. For the Commission to approve rule changes proposed by a registered securities association (*e.g.*, FINRA) the proposed rule changes must be consistent with the requirements of the Exchange Act, including Section 15A(b)(6) of the Act,[29] and the rules and regulations thereunder. Section 15A(b)(6) requires that the rules of a registered securities association be, ''designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, to fix minimum profits, to impose any schedule or fix rates of commissions, allowances, discounts, or other fees to be charged by its members, or to regulate by virtue of any authority conferred by [Section 15A] matters not related to the purposes of [Section 15A] or the administration of the association.''

The over-the-counter (''OTC'') market for CDS has been a source of concerns to the Commission and other financial regulators.[30] These concerns include the systemic risk posed by CDS, highlighted by the possible inability of parties to meet their obligations as counterparties and the potential resulting adverse effects on other markets and the financial system.[31] Recent credit market events have demonstrated the seriousness of these risks in a CDS market operating without meaningful regulation, transparency,[32] or central clearing counterparties.[33] These events have emphasized the need for central clearing counterparties as mechanisms to help control such risks.[34] Establishment of central clearing counterparties for CDS is expected to reduce the counterparty risks inherent in the CDS market, and thereby help mitigate potential systemic impacts. As we have stated previously,[35] given the continued uncertainty in this market, taking action to help foster the prompt development of central clearing counterparties is in the public interest.

The Commission believes that using well-regulated central clearing counterparties to clear transactions in CDS helps promote efficiency and reduce risk in the CDS market and among its participants.[36] These benefits can be particularly significant in times of market stress, as central clearing counterparties can mitigate the potential for a market participant's failure to destabilize other market participants, and reduce the effects of misinformation and rumors.[37] Central clearing counterparty-maintained records of CDS transactions may also aid the Commission's efforts to prevent and detect fraud and other abusive market practices.[38]

Well-regulated central clearing counterparties also are expected to address concerns about counterparty risk by substituting the creditworthiness and liquidity of the central clearing counterparties for the creditworthiness and liquidity of the counterparties to a CDS.[39] In the absence of central clearing counterparties, participants in the OTC CDS market must carefully manage their counterparty risks because a default by a counterparty can render worthless, and payment delay can reduce the usefulness of, the credit protection that has been bought by a CDS purchaser.[40] Firms that trade CDS OTC attempt to manage counterparty risk by carefully selecting and monitoring their counterparties, entering into legal agreements that permit them to net gains and losses across contracts with a defaulting counterparty, and often requiring counterparty exposures to be collateralized.[41] Central clearing

[27] 15 U.S.C. 78*o*–3(b)(6).

[28] 15 U.S.C. 78s(b)(2).

[29] 15 U.S.C. 78*o*–3(b)(6).

[30] *See* Securities Exchange Act Releases Nos. 59164, p. 1 (Dec. 24, 2008), 74 FR 139 (Jan. 2, 2009), 59165, p. 1 (Dec. 24, 2008), 74 FR 133 (Jan. 2, 2009), 59527, p. 1 (Mar. 6, 2009), 74 FR 10791 (Mar. 12, 2009), 59578, p. 1 (Mar 13, 2009), 74 FR 11781, at 11782 (Mar. 19, 2009), and Securities Act Release No. 8999, p. 4 (Jan. 14, 2009), 74 FR 3967 (Jan. 22, 2009).

[31] *Id.* In addition to the potential systemic risks that CDS pose to financial stability, we are concerned about other potential risks in this market, including operational risks, risks relating to manipulation and fraud, and regulatory arbitrage risks.

[32] *See* Policy Objectives for the OTC Derivatives Market, The President's Working Group on Financial Markets, November 14, 2008, available at *http://www.ustreas.gov/press/releases/reports/policyobjectives.pdf* (''Public reporting of prices, trading volumes and aggregate open interest should be required to increase market transparency for participants and the public.'').

[33] *See* The Role of Credit Derivatives in the U.S. Economy Before the H. Agric. Comm., 110th Cong. (2008) (Statement of Erik Sirri, Director of the Division of Trading and Markets, Commission).

[34] *See id.*

[35] *See* Securities Exchange Act Release Nos. 59164 (Dec. 24, 2008), 74 FR 139 (Jan. 2, 2009), 59527 (Mar. 6, 2009), 74 FR 10791 (Mar. 12, 2009), and 59578 (Mar. 13, 2009), 74 FR 11781 (Mar. 19, 2009).

[36] *See* Securities Exchange Act Releases Nos. 59164, p. 4 (Dec. 24, 2008), 74 FR 139, at 140 (Jan. 2, 2009), 59527, p. 4 (Mar. 6, 2009), 74 FR 10791, at 10792 (Mar. 12, 2009), and 59578, p. 4 (Mar. 13, 2009), 74 FR 11781, at 11782 (Mar. 19, 2009).

[37] *Id.*

[38] *Id.*

[39] *Id.*

[40] *Id.*

[41] *See generally* R. Bliss and C. Papathanassiou, ''Derivatives clearing, central counterparties and novation: The economic implications,'' *http://www.ecb.int/events/pdf/conferences/ccp/BlissPapathanassiou_final.pdf* (Mar. 8, 2006), at 6.

Continued

counterparties are expected to allow participants to avoid the risks specific to individual counterparties because central clearing counterparties generally ''novate'' bilateral trades by entering into separate contractual arrangements with both counterparties—becoming buyer to one and seller to the other.[42] Through novation, it is the central clearing counterparty that assumes the counterparty risks. For this reason, central clearing counterparties for CDS are expected to contribute generally to the goal of market stability.[43] As part of its risk management, a central clearing counterparty may subject novated contracts to initial and variation margin requirements and establish a clearing fund.[44] A central clearing counterparty also may implement a loss-sharing arrangement among its participants to respond to a participant insolvency or default.[45]

Central clearing counterparties also are expected to reduce CDS risks through multilateral netting of trades.[46] Trades cleared through a central clearing counterparty would limit a participant's exposure to an OTC market dealer, permitting the participant to accept the best bid or offer in the OTC market regardless of the creditworthiness of the dealer.[47] In addition, by allowing netting of positions in similar instruments, and netting of gains and losses across different instruments, central clearing counterparties are expected to reduce redundant notional exposures and promote the more efficient use of resources for monitoring and managing CDS positions.[48] Through risk controls, including controls on market-wide concentrations that cannot be implemented effectively when counterparty risk management is decentralized, central clearing counterparties are expected to help prevent a single market participant's failure from destabilizing other market participants and, ultimately, the broader financial system.[49]

After careful consideration, the Commission finds that FINRA's proposed rule change to establish a pilot program implementing minimum customer margin requirements for transactions in CDS is consistent with the requirements of the Exchange Act,[50] including Section 15A(b)(6) of the Act.[51] In particular, the Commission finds that FINRA's proposed rule is consistent with Section 15A(b)(6) of the Act[52] in that it is designed to perfect the mechanism of a free and open market and to protect investors and the public interest. The Commission notes that the proposed rule is intended to promote greater accuracy and efficiency with respect to Exchange margin requirements. The proposed rule is intended to align a customer's total margin requirement for CDS positions with the actual risk associated with those positions taken as a whole. FINRA's proposed rule also is consistent with 15A(b)(6) of the Act[53] because it is designed to limit the amount of leverage a customer can obtain though CDS positions and decreases the risk that a broker-dealer will fail because its customers are unable to fulfill their obligations to the firm.

The Commission also finds that accelerated approval is appropriate. More specifically, accelerated approval will allow the pilot program, which will expire on September 25, 2009, to be in effect for a sufficient period of time to permit FINRA to properly evaluate the performance of the margin rule so that it can propose suitable permanent margin rules for CDS. Further, accelerated approval is appropriate because it will enable the CME to immediately begin clearing customer, in addition to proprietary, CDS positions, and therefore, enable market participants to receive more quickly the benefits described above, such as increased market stability, arising from the existence of a well-regulated central clearing counterparty.

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.* Please include File Number SR–FINRA–2009–012 on the subject line.

Paper Comments

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

All submissions should refer to File Number SR–FINRA–2009–012. 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

See also ''New Developments in Clearing and Settlement Arrangements for OTC Derivatives,'' Committee on Payment and Settlement Systems, BIS, at 25 (Mar. 2007), available at *http://www.bis.org/pub/cpss77.pdf*; ''Reducing Risks and Improving Oversight in the OTC Credit Derivatives Market,'' Before the Sen. Subcomm. On Secs., Ins. and Investments, 110th Cong. (2008) (Statement of Patrick Parkinson, Deputy Director, Division of Research and Statistics, FRB).

[42] *See* Securities Exchange Act Releases Nos. 59164, p. 4 (Dec. 24, 2008), 74 FR 139, at 140 (Jan. 2, 2009), 59527, p. 4 (Mar. 6, 2009), 74 FR 10791, at 10792 (Mar. 12, 2009), and 59578, p. 4 (Mar. 13, 2009), 74 FR 11781, at 11782 (Mar. 19, 2009). ''Novation'' is a ''process through which the original obligation between a buyer and seller is discharged through the substitution of the central clearing counterparty as seller to buyer and buyer to seller, creating two new contracts.'' Committee on Payment and Settlement Systems, Technical Committee of the International Organization of Securities Commissioners, Recommendations for Central Counterparties (November 2004) at 66.

[43] *See* Securities Exchange Act Releases Nos. 59164, p. 5 (Dec. 24, 2008), 74 FR 139, at 140 (Jan. 2, 2009), 59527, p. 5 (Mar. 6, 2009), 74 FR 10791, at 10792 (Mar. 12, 2009), and 59578, p. 5 (Mar. 13, 2009), 74 FR 11781, at 11782 (Mar. 19, 2009).

[44] *Id.*

[45] *Id.*

[46] *See* Securities Exchange Act Releases Nos. 59164, p. 5 (Dec. 24, 2008), 74 FR 139, at 140 (Jan. 2, 2009), 59527, p. 5 (Mar. 6, 2009), 74 FR 10791, at 10792 (Mar. 12, 2009), and 59578, p. 5 (Mar. 13, 2009), 74 FR 11781, at 11782 (Mar. 19, 2009). *See also,* ''New Developments in Clearing and Settlement Arrangements for OTC Derivatives,'' *supra* note 11, at 25. Multilateral netting of trades would permit multiple counterparties to offset their open transaction exposure through the central clearing counterparty, spreading credit risk across all participants in the clearing system and more effectively diffusing the risk of a counterparty's default than could be accomplished by bilateral netting alone.

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] In approving this proposed rule change, the Commission has considered its impact on efficiency, competition, and capital formation. *See* 15 U.S.C. 78c(f).

[51] 15 U.S.C. 78o–3(b)(6).

[52] *Id.*

[53] *Id.*

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–2009–012 and should be submitted on or before June 18, 2009.

V. Conclusion

For the foregoing reasons, pursuant to Section 19(b)(2) of the Act,[54] the Commission finds good cause to approve the proposed rule change on an accelerated basis.

It is hereby ordered, pursuant to Section 19(b)(2) of the Act, that the proposed rule change (SR–FINRA–2009–012) be, and it hereby is, approved on an accelerated basis to establish an interim pilot program expiring on September 25, 2009.

By the Commission.

Elizabeth M. Murphy,

Secretary.

[FR Doc. E9–12342 Filed 5–27–09; 8:45 am]

BILLING CODE 8010–01–P

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–59949; File No. SR–ISE–2007–97]

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Approving Proposed Rule Change, as Modified by Amendment No. 1, Relating to Market Data Fees

May 20, 2009.

I. Introduction

On October 5, 2007, International Securities Exchange, LLC (the ''Exchange'' or ''ISE'') filed with the Securities and Exchange Commission (''Commission''), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'')[1] and Rule 19b–4 thereunder,[2] a proposed rule change to establish fees for a real-time depth of market data offering. On March 9, 2009, the Exchange filed Amendment No. 1 to the proposed rule change. The proposed rule change, as modified by Amendment No. 1, was published for comment in the **Federal Register** on April 7, 2009.[3] The Commission received no comments on the proposal. This order approves the proposed rule change, as modified by Amendment No. 1.

II. Description of the Proposal

The Exchange currently produces and provides free of charge a data feed that contains the aggregate bid and offer size available at the first five price levels on ISE's limit order book, the ISE Depth of Market Data Feed (''Depth of Market''). The Depth of Market feed includes non-marketable orders and quotes that are displayed, and is distributed in real time.

ISE has proposed to establish fees for its Depth of Market product. ISE will make this product available to members and non-members, and to professional and non-professional subscribers. Specifically, the Exchange proposes to charge distributors of Depth of Market $5,000 per month.[4] In addition, the Exchange proposes to charge each distributor a monthly fee per controlled device[5] of $50 per controlled device for Professionals (for internal use or external redistribution through a controlled device) and $5 per controlled device for Non-Professionals who receive the data from a distributor through a controlled device.[6] ISE proposes to cap the monthly maximum amount of fees payable by a distributor at $7,500 for Professionals where the data is for internal use only; $12,500 for Professionals where the data is redistributed externally; and $10,000 for Non-Professionals who receive the data from a distributor. The Exchange proposes to charge distributors a flat fee of $1,000 for the first month after connectivity has been established between ISE and the distributor. Further, the Exchange proposes to waive all user fees during this one month period.

III. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange.[7] In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(4) of the Act,[8] which requires that the rules of a national securities exchange provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other parties using its facilities, and Section 6(b)(5) of the Act,[9] which requires, among other things, that the rules of an exchange be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest, and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers. The Commission also finds that the proposed rule change is consistent with Section 6(b)(8) of the Act[10] in that it does not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act.

The Commission has reviewed the proposal using the approach set forth in the NYSE Arca Order for non-core market data fees.[11] In the NYSE Arca Order, the Commission stated that ''when possible, reliance on competitive forces is the most appropriate and effective means to assess whether the terms for the distribution of non-core data are equitable, fair and reasonable, and not unreasonably discriminatory.''[12] It noted that the ''existence of significant competition provides a substantial basis for finding that the terms of an exchange's fee proposal are equitable, fair, reasonable, and not unreasonably or unfairly discriminatory.''[13] If an exchange ''was subject to significant competitive forces in setting the terms of a proposal,'' the Commission will approve a proposal unless it determines that ''there is a substantial countervailing basis to find that the terms nevertheless fail to meet an applicable requirement of the Exchange Act or the rules thereunder.''[14]

---

[54] 15 U.S.C. 78s(b)(2).

[1] 15 U.S.C. 78s(b)(1).

[2] 17 CFR 240.19b–4.

[3] *See* Securities Exchange Act Release No. 59679 (April 1, 2009), 74 FR 15795 (''Notice'').

[4] A ''distributor'' will be defined as any firm that receives an ISE data feed directly from ISE or indirectly through a ''redistributor'' and then distributes it either internally or externally. ISE proposes that all distributors execute an ISE distributor agreement. ''Redistributors'' will include market data vendors and connectivity providers such as extranets and private network providers.

[5] A ''controlled device'' is defined as any device that a distributor of the ISE Depth of Market permits to access the information in the Depth of Market offering.

[6] In differentiating between a ''Non-Professional Subscriber'' and a ''Professional Subscriber,'' ISE will apply the same criteria for qualification as in the Consolidated Tape Association Plan (''CTA Plan'') and the Consolidated Quotation Plan (''CQ Plan'').

[7] 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).

[8] 15 U.S.C. 78f(b)(4).

[9] 15 U.S.C. 78f(b)(5).

[10] U.S.C. 78f(b)(8).

[11] *See* Securities Exchange Act Release No. 59039 (December 2, 2008), 73 FR 74770 (December 9, 2008) (SR–NYSEArca–2006–21) (''NYSE Arca Order'').

[12] *Id.* at 74771.

[13] *Id.* at 74782.

[14] *Id.* at 74781.