narrow-based security index composed of such securities.

[71 FR 39543, July 13, 2006]

§ 240.7c2–1 [Reserved]

HYPOTHECATION OF CUSTOMERS' SECURITIES

§ 240.8c–1 Hypothecation of customers' securities.

(a) *General provisions.* No member of a national securities exchange, and no broker or dealer who transacts a business in securities through the medium of any such member shall, directly or indirectly, hypothecate or arrange for or permit the continued hypothecation of any securities carried for the account of any customer under circumstances:

(1) That will permit the commingling of securities carried for the account of any such customer with securities carried for the account of any other customer, without first obtaining the written consent of each such customer to such hypothecation;

(2) That will permit such securities to be commingled with securities carried for the account of any person other than a bona fide customer of such member, broker or dealer under a lien for a loan made to such member, broker or dealer; or

(3) That will permit securities carried for the account of customers to be hypothecated or subjected to any lien or liens or claim or claims of the pledges or pledgees, for a sum which exceeds the aggregate indebtedness of all customers in respect of securities carried for their accounts; except that this clause shall not be deemed to be violated by reason of an excess arising on any day through the reduction of the aggregate indebtedness of customers on such day, provided that funds or securities in an amount sufficient to eliminate such excess are paid or placed in transfer to pledgees for the purpose of reducing the sum of the liens or claims to which securities carried for the account of customers are subjected as promptly as practicable after such reduction occurs, but before the lapse of one-half hour after the commencement of banking hours on the next banking day at the place where the largest principal amount of loans of such member, broker or dealer are payable and, in any event, before such member, broker or dealer on such day has obtained or increased any bank loan collateralized by securities carried for the account of customers.

(b) *Definitions.* For the purposes of this section:

(1) The term *customer* shall not include any general or special partner or any director or officer of such member, broker or dealer, or any participant, as such, in any joint, group or syndicate account with such member, broker or dealer or with any partner, officer or director thereof. The term also shall not include any counterparty who has delivered collateral to an OTC derivatives dealer pursuant to a transaction in an eligible OTC derivative instrument, or pursuant to the OTC derivatives dealer's cash management securities activities or ancillary portfolio management securities activities, and who has received a prominent written notice from the OTC derivatives dealer that:

(i) Except as otherwise agreed in writing by the OTC derivatives dealer and the counterparty, the dealer may repledge or otherwise use the collateral in its business;

(ii) In the event of the OTC derivatives dealer's failure, the counterparty will likely be considered an unsecured creditor of the dealer as to that collateral;

(iii) The Securities Investor Protection Act of 1970 (15 U.S.C. 78aaa through 78lll) does not protect the counterparty; and

(iv) The collateral will not be subject to the requirements of § 240.8c–1, § 240.15c2–1, § 240.15c3–2, or § 240.15c3–3;

(2) The term *securities carried for the account of any customer* shall be deemed to mean:

(i) Securities received by or on behalf of such member, broker or dealer for the account of any customer;

(ii) Securities sold and appropriated by such member, broker or dealer to a customer, except that if such securities were subject to a lien when appropriated to a customer they shall not be deemed to be ''securities carried for the account of any customer'' pending

their release from such lien as promptly as practicable:

(iii) Securities sold, but not appropriated, by such member, broker or dealer to a customer who has made any payment therefor, to the extent that such member, broker or dealer owns and has received delivery of securities of like kind, except that if such securities were subject to a lien when such payment was made they shall not be deemed to be ''securities carried for the account of any customer'' pending their release from such lien as promptly as practicable:

(3) ''Aggregate indebtedness'' shall not be deemed to be reduced by reason of uncollected items. In computing aggregate indebtedness, related guaranteed and guarantor accounts shall be treated as a single account and considered on a consolidated basis, and balances in accounts carrying both long and short positions shall be adjusted by treating the market value of the securities required to cover such short positions as though such market value were a debit; and

(4) In computing the sum of the liens or claims to which securities carried for the account of customers of a member, broker or dealer are subject, any rehypothecation of such securities by another member, broker or dealer who is subject to this section or to § 240.15c2–1 shall be disregarded.

(c) *Exemption for cash accounts.* The provisions of paragraph (a)(1) of this section shall not apply to any hypothecation of securities carried for the account of a customer in a special cash account within the meaning of 12 CFR 220.4(c): *Provided,* That at or before the completion of the transaction of purchase of such securities for, or of sale of such securities to, such customer, written notice is given or sent to such customer disclosing that such securities are or may be hypothecated under circumstances which will permit the commingling thereof with securities carried for the account of other customers. The term *the completion of the transaction* shall have the meaning given to such term by § 240.15c1–1(b).

(d) *Exemption for clearinghouse liens.* The provisions of paragraphs (a)(2), (a)(3), and (f) of this section shall not apply to any lien or claim of the clearing corporation, or similar department or association, of a national securities exchange or a registered national securities association for a loan made and to be repaid on the same calendar day, which is incidental to the clearing of transactions in securities or loans through such corporation, department, or association: *Provided, however,* That for the purpose of paragraph (a)(3) of this section, ''aggregate indebtedness of all customers in respect of securities carried for their accounts'' shall not include indebtedness in respect of any securities subject to any lien or claim exempted by this paragraph.

(e) *Exemption for certain liens on securities of noncustomers.* The provisions of paragraph (a)(2) of this section shall not be deemed to prevent such member, broker or dealer from permitting securities not carried for the account of a customer to be subjected (1) to a lien for a loan made against securities carried for the account of customers, or (2) to a lien for a loan made and to be repaid on the same calendar day. For the purpose of this exemption, a loan shall be deemed to be ''made against securities carried for the account of customers'' if only securities carried for the account of customers are used to obtain or to increase such loan or as substitutes for other securities carried for the account of customers.

(f) *Notice and certification requirements.* No person subject to this section shall hypothecate any security carried for the account of a customer unless at or prior to the time of each such hypothecation, he gives written notice to the pledgee that the security pledged is carried for the account of a customer and that such hypothecation does not contravene any provision of this section, except that in the case of an omnibus account the members, broker or dealer for whom such account is carried may furnish a signed statement to the person carrying such account that all securities carried therein by such member, broker or dealer will be securities carried for the account of his customers and that the hypothecation thereof by such member, broker or dealer will not contravene any provision of this section. The provisions of this paragraph shall

not apply to any hypothecation of securities under any lien or claim of a pledgee securing a loan made and to be repaid on the same calendar day.

(g) The fact that securities carried for the accounts of customers and securities carried for the accounts of others are represented by one or more certificates in the custody of a clearing corporation or other subsidiary organization of either a national securities exchange or of a registered national securities association, or of a custodian bank, in accordance with a system for the central handling of securities established by a national securities exchange or a registered national securities association, pursuant to which system the hypothecation of such securities is effected by bookkeeping entries without physical delivery of such securities, shall not, in and of itself, result in a commingling of securities prohibited by paragraph (a)(1) or (a)(2) of this section, whenever a participating member, broker or dealer hypothecates securities in accordance with such system: *Provided, however,* That (1) any such custodian of any securities held by or for such system shall agree that it will not for any reason, including the assertion of any claim, right or lien of any kind, refuse to refrain from promptly delivering any such securities (other than securities then hypothecated in accordance with such system) to such clearing corporation or other subsidiary organization or as directed by it, except that nothing in such agreement shall be deemed to require the custodian to deliver any securities in contravention of any notice of levy, seizure or similar notice, or order or judgment, issued or directed by a governmental agency or court, or officer thereof, having jurisdiction over such custodian, which on its face affects such securities; (2) such systems shall have safeguards in the handling, transfer and delivery of securities and provisions for fidelity bond coverage of the employees and agents of the clearing corporation or other subsidiary organization and for periodic examinations by independent public accountants; and (3) the provisions of this paragraph shall not be effective with respect to any particular system unless the agreement required by paragraph (g)(1) of this section and the safeguards and provisions required by paragraph (g)(2) of this section shall have been deemed adequate by the Commission for the protection of investors, and unless any subsequent amendments to such agreement, safeguards or provisions shall have been deemed adequate by the Commission for the protection of investors.

(Secs. 3, 8, 15, 48 Stat. 882, 888, 895; 15 U.S.C. 78c, 78h, 78*o*)

CROSS REFERENCE: For interpretative releases applicable to § 240.8c–1, see Nos. 2690 and 2822 in tabulation, part 241 of this chapter.

[13 FR 8180, Dec. 22, 1948, as amended at 31 FR 7740, June 1, 1966; 37 FR 73, Jan. 5, 1973; 63 FR 59395, Nov. 3, 1998]

§ 240.9b–1 Options disclosure document.

(a) *Definitions.* The following definitions shall apply for the purpose of this rule.

(1) *Options market* means a national securities exchange, an automated quotation system of a registered securities association or a foreign securities exchange on which standardized options are traded.

(2) *Options class* means all options contracts covering the same underlying instrument.

(3) *Options disclosure document* means a document, including all amendments and supplements thereto, prepared by one or more options markets which has been filed with the Commission or distributed in accordance with paragraph (b) of this section. *Definitive options disclosure document* or *document* means an options disclosure document furnished to customers in accordance with paragraph (b) of this section.

(4) *Standardized options* are options contracts trading on a national securities exchange, an automated quotation system of a registered securities association, or a foreign securities exchange which relate to options classes the terms of which are limited to specific expiration dates and exercise prices, or such other securities as the Commission may, by order, designate.

(b)(1) Five preliminary copies of an options disclosure document containing the information specified in paragraph (c) of this section shall be