No. 11-___

IN THE

Supreme Court of the United States

STANDARD INVESTMENT CHARTERED, INC.,
ON BEHALF OF ITSELF AND ALL OTHERS
SIMILARLY SITUATED,

Petitioner,

v.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, ET AL.,

Respondents.

On Petition for a Writ of Certiorari to the
United States Court of Appeals for the Second Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Respondent National Association of Securities Dealers (NASD) is a private entity that engages in proprietary activities as well as certain regulatory activities of its members as a so-called "Self Regulatory Organization" (SRO). Petitioner, a securities dealer, is a NASD member. Petitioner and other members lost significant voting control over NASD through a proxy solicitation. Petitioner then brought this state-law suit alleging that NASD had lied to the membership in the proxy statement by significantly understating the compensation they could legally receive in exchange for giving up their voting rights.

The Second Circuit held, in conflict with other circuits, that SROs have absolute, non-statutory immunity for any illegal acts that are "incident to" their regulatory activities. In this case, the court reasoned, the voting-rights changes were "incident to" NASD's regulatory activities because they were part of a broader plan by NASD to acquire assets from a competitor and form a larger entity that would also have certain SRO responsibilities.

The Question Presented is:

Are SROs entitled to absolute immunity for unlawful conduct that is "incident to" their regulatory powers but does not involve performance of any regulatory duty on behalf of the government?

PARTIES TO THE PROCEEDING

Petitioner is Standard Investment Chartered, Inc., individually and on behalf of all others similarly situated.

Respondents are the National Association of Securities Dealers, Inc., a/k/a NASD, Richard F. Brueckner, Barbara Z. Sweeney, Financial Industry Regulatory Authority, Inc., a/k/a/ FINRA, T. Grant Callery, Todd Diganci, Mary L. Schapiro, and Howard M. Schloss.

NYSE Group, Inc., was a defendant below, but petitioner does not seek review of its dismissal from the case.

RULE 29.6 DISCLOSURE

Standard Investment Chartered, Inc., has no parent corporation, and no person or publicly-traded corporation owns more than 10% of the company's stock.

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PETITION FOR A WRIT OF CERTIORARI

Petitioner Standard Investment Chartered, Inc., on behalf of itself and all others similarly situated, respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit.

OPINIONS BELOW

The opinion of the United States Court of Appeals for the Second Circuit (Pet. App. 1a-8a) is reported at 637 F.3d 112 (2d Cir. 2011). The Second Circuit's order denying rehearing en banc (Pet. App. 16a-17a) is unreported. The opinion of the district court (Pet. App. 9a-12a) is unreported but available at 2010 WL 749844.

JURISDICTION

The Second Circuit issued its decision on February 22, 2011, and denied rehearing on April 25, 2011. Pet. App. 16a. Justice Ginsburg extended the time to file this petition up to and including September 22, 2011. No. 11A62. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

RELEVANT STATUTORY PROVISIONS

Relevant portions of the Securities Exchange Act, 15 U.S.C. §§ 78a-78pp, are reproduced at Pet. App. 18a-33a.

STATEMENT OF THE CASE

Petitioner is a California financial services provider and a member of the National Association of

Securities Dealers (NASD).[1] NASD is a private, non-governmental organization that also exercises certain regulatory powers over its members as a Self Regulatory Organization (SRO). In 2006, NASD sought to acquire particular assets of the New York Stock Exchange (NYSE). The deal required an amendment to NASD's bylaws that would increase the voting power of the NYSE's large institutional members at the expense of NASD's existing, smaller members like petitioner. The amendment, in turn, required approval by NASD's membership.

Petitioner subsequently filed this state-law suit, alleging that NASD's proxy statement seeking approval of the bylaw amendments was fraudulent. The Second Circuit held that NASD was entitled to absolute immunity. Although NASD was not exercising any regulatory power when it made the misrepresentations, or more broadly when it weakened the voting power of its existing members, the Second Circuit held, in conflict with three other circuits, that SROs are absolutely immune from liability for any conduct that is "incident to" the exercise of regulatory power. Pet. App. 7a.

I. Statutory Background

Respondent NASD is a privately-held Delaware non-profit corporation with more than three thousand employees across the country. NASD regularly conducts proprietary activities designed to

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[1] NASD has changed its name to the Financial Industry Regulatory Authority (FINRA). This petition refers to respondent by the name it held when the suit was initiated.

further its own institutional interests. For instance, NASD assesses and collects annual fees from its member organizations, manages its financial accounts, and rents and owns property. It has also traditionally engaged in private revenue-generating enterprises, most notably including the for-profit NASDAQ stock exchange that it created and ultimately spun off in an initial public offering that raised $1.5 billion in equity. Complaint ¶ 58. In recognition of these proprietary interests, NASD's corporate charter declares that one of its purposes is "[t]o transact business and to purchase, hold, own, lease, mortgage, sell, and convey any and all property, real and personal, necessary, convenient, or useful for the purposes of the Corporation." Restated Certificate of Incorporation of FINRA, Inc.[2]

NASD is also registered as an SRO. Pet. App. 3a. Congress recognized SROs in the Securities Exchange Act of 1934, which created a dual public-private regulatory system whereby private stock exchanges and securities associations would be required to register with the SEC, enact rules to protect investors, and discipline their members. *See, e.g.*, 15 U.S.C. §§ 78s, 78o-3. Nothing in the Exchange Act establishes absolute immunity for the SROs from private lawsuits. Nor does the Act provide government regulators with carte blanche authority to oversee the SROs with respect to their proprietary activities; it instead provides targeted government oversight over the SROs in the performance of their

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[2] *Available at* http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=4589.

regulatory duties. *See*, *e.g.*, 15 U.S.C. §§ 78s(d)(1), (2) (subjecting to SEC review only those SRO actions involving membership, discipline, and service provision).

Accordingly, like other SROs, NASD wears two hats. On some occasions, it exercises regulatory authority over its members' activities in securities markets, the kind of authority that might otherwise be exercised by a government agency. But on other occasions, it attends to its private, proprietary interests – renting facilities, hiring employees, acquiring assets, paying bonuses to its management, and dealing with questions of corporate governance. In their proprietary capacity, SROs are similar to other corporations, their conduct toward their members being the *subject* of regulation, rather than constituting an *act* of delegated regulatory authority.

For that reason, unlike government regulators, SROs are answerable in significant degree to their members, for whom they often hold considerable assets. At the time this lawsuit was filed, for instance, NASD held more than $1.5 billion in "members equity" on its balance sheets. Complaint ¶ 59.

II. Factual Background

In 2006, NASD undertook to use its members' assets to purchase the regulatory arm of the New York Stock Exchange (NYSE). Pet. App. 3a. The acquisition would serve several of NASD's proprietary objectives, such as increasing the revenue base for membership dues, eliminating a competing regulator, and triggering substantial bonuses for several NASD officers, Complaint ¶ 14.

As a condition to agreeing to the sale, the NYSE insisted that NASD amend its bylaws to abandon its "one member, one vote" system in favor of a new voting structure that assigned votes based upon the size of the member firm.[3] Pet. App. 3a-4a. The bylaw change was thus not in any respect a regulatory condition of the acquisition. Rather the two private parties to the transaction themselves deemed it a prerequisite, and they did so in order to protect the private interests of the NYSE's members. Complaint ¶ 56.

The bylaw amendment required NASD member approval. In an attempt to secure the support of smaller members like petitioner, NASD offered a one-time "special member payment" of $35,000. Pet. App. 4a. The proxy solicitation statement represented that "a larger payment is not possible" due to limitations imposed by the IRS. Complaint ¶ 13. Respondent repeated this representation during a month-long, twenty-six city "road show" program to solicit member approval of the bylaw changes. *Id*. ¶¶ 107, 112.

In fact, IRS rules would have permitted NASD to pay petitioner and other NASD members much more in exchange for approval of the bylaw change.[4]

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[3] The "one member, one vote" system existed to ensure that officer elections, committee membership assignments, and decisions regarding other proprietary NASD functions would be made on a "democratic basis." Exchange Act Release No. 2045, 1939 SEC LEXIS 66, at *4 (Mar. 20, 1939).

[4] NASD produced documents to petitioner that bear on the truthfulness of the proxy statements. Those documents, and the

Complaint ¶¶ 6, 16, 33, 96. Several of respondent's other statements and omissions were misleading as well. For instance, the proxy statement failed to mention that NASD officers had a major financial incentive for promoting the change, which would entitle them to hundreds of thousands of dollars in bonuses. *Id*. ¶ 15, 16. The proxy statement also failed to disclose that NASD and NYSE had discussed and rejected an alternative form to the transaction whereby rather than merging the NYSE assets into NASD, NASD would be dissolved and then reformed with the NYSE assets as a new entity altogether. *Id*. ¶¶ 16, 135. If NASD had done so, the *entirety* of the members' equity could have been vested in the members upon dissolution, totaling roughly $300,000 per firm as opposed to the $35,000 offered in the special member payment. *Id*. ¶¶ 19, 34.

Unaware of these misrepresentations and omissions, and therefore believing that the bylaw revision was being approved on the best possible terms for the members who whose voting rights would be diluted, NASD members voted their approval on January 19, 2007. Pet. App. 4a. NASD then submitted the proposed bylaw changes to the SEC, seeking its affirmation that the changes were consistent with the Exchange Act. Notably, neither NASD's submission to the SEC nor the SEC's notice seeking public comment on the proposed bylaw change gave any indication that the SEC would even

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actual amount of the maximum permissible payment, were placed under seal at NASD's insistence.

consider issues related to the proxy solicitation (as opposed to the bylaw change) during the SEC's approval process. Complaint ¶ 74.

III. Procedural History

1. In March 2007, petitioner filed this diversity action asserting state law fraud claims.

The district court initially dismissed the action, holding that petitioner was first required to exhaust administrative remedies by challenging the bylaw amendment before the SEC. *Standard Inv. Chartered v. Nat'l Ass'n of Sec. Dealers, Inc.*, No. 07 Civ. 2014, 2007 WL 1296712 (S.D.N.Y. May 2, 2007). Petitioner then submitted its substantive claims to the SEC, asserting that NASD had obtained approval of its bylaw changes through a fraudulent proxy statement and other misleading statements and omissions, in violation of state law. Petitioner repeatedly asked the SEC to review documents bearing on NASD's fraudulent misrepresentations, but the SEC refused to do so. Complaint ¶¶ 76-80. Instead, the SEC ultimately approved the bylaw amendments, explaining that it "ordinarily does not make determinations regarding state law issues." Exchange Act Release No. 56145, 72 Fed. Reg. 42169, 42188 (July 26, 2007) ("Approval Order").

Petitioner appealed the SEC's order to the Ninth Circuit, asking that court to make clear that petitioner would be permitted to proceed on its fraud claim free from any preclusion defenses. Complaint ¶ 84. In response, the SEC requested a remand to the agency to allow it to clarify its order. *Id*. ¶ 85. The SEC explained to the court of appeals that its Approval Order did "not purport to decide a question

of state law" or bind courts in a subsequent action. *Id*. The Ninth Circuit granted the motion.

On remand, over NASD's objection, the SEC issued a new order clarifying that in approving respondent's bylaw change, the SEC did not issue "a definitive adjudication under state law" regarding petitioner's "claim that the proxy statement was misleading." Exchange Act Release No. 56145A, 73 Fed. Reg. 32377, 32377 (May 30, 2008). The SEC explained further that its approval order was only meant to confirm that the "NASD complied with its Certificate of Incorporation and by-laws" with respect to the proxy process. *Id*. The SEC's clarified position thus explained why the Commission had refused to even consider evidence bearing on respondents' fraudulent conduct: the Commission simply refused to decide the substance of petitioner's fraud claims. This position was in line with the SEC's traditional interpretation of its own limited authority to regulate SRO behavior. *See, e.g.*, Exchange Act Release No. 51252, 70 Fed. Reg. 10442, 10444 (Feb. 25, 2005) (SEC does not purport to decide questions of state law).

2. Having exhausted the administrative process before the SEC, petitioner renewed its original action in the district court in New York.

The district court again dismissed, this time holding on the basis of a long line of decisions in the Second Circuit that NASD was entitled to absolute immunity for "acts and forbearances [that were] *incident to* the exercise of regulatory power." Pet. App. 11a (emphasis added). The court did not dispute that NASD's actions were pursuant to and furthered its private, proprietary interests, and that

nothing in the Exchange Act required NASD to acquire the assets of its competitor, much less authorized it to secure membership approval of bylaw changes through false statements. Nor did the court find that issuing the false proxy solicitations was an exercise of a delegated regulatory power that would otherwise have been undertaken by the SEC. The court instead deemed it sufficient for the purpose of triggering immunity that the false proxy statement was issued in order to secure approval of a bylaw amendment that NASD and NYSE had privately agreed would be required to conclude their consolidation and that the result of the consolidation would be a new SRO with expanded membership. *Id*. 12a.

3. The Second Circuit affirmed. The court agreed with the district court that the regulatory *consolidation* – which the SEC had reviewed and approved – was "on its face, an exercise of the SRO's delegated regulatory functions and thus entitled to immunity." Pet. App. 7a. But the court recognized that the real "question confronting the court" was whether immunity should also attach to the "proxy solicitation regarding amendments to the bylaws," which was only "incident to the consolidation" (and which the SEC had *not* reviewed or approved). *Id*. The court acknowledged that such conduct did not fall within the traditionally recognized categories of immunized SRO regulatory action, such as "disciplinary proceedings," "enforcement of security rules and regulations," "the interpretation of securities laws and regulations," "referral of exchange members to the SEC," or "the public announcement of regulatory decisions." *Id*. 5a (citations omitted).

Nonetheless, although issuing proxy statements was neither an exercise of delegated regulatory authority nor subject to SEC review regarding claims of state law fraud, the court concluded that NASD was entitled to immunity under the Second Circuit's broad protection of any conduct that is "incident to the exercise of regulatory power." Pet. App. 7a (quoting *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 98 (2d Cir. 2007)). The court of appeals agreed with the district court that the proxy statement was "incident to" the exercise of regulatory authority because it was a "prerequisite to the completion of [the] consolidation" of NASD and NYSE's regulatory functions, and because the Exchange Act treats SRO bylaw amendments – even if not proxy solicitations – as a form of rulemaking subject to SEC oversight and approval. *Id*.

5. Petitioner filed a petition for rehearing en banc, which was denied on April 25, 2011. Pet. App. 16a. This petition followed.

REASONS FOR GRANTING THE WRIT

As the U.S. Chamber of Commerce has recently observed, the "level of accountability" that SROs show to their constituents has simply "not kept pace" with the SROs' increasing influence over financial markets – particularly as many have transformed into for-profit entities. CENTER FOR CAPITAL MARKETS COMPETITIVENESS, U.S. CAPITAL MARKETS COMPETITIVENESS: THE UNFINISHED AGENDA 21 (2011). The Second Circuit's decision in this case exacerbates this serious problem by establishing a dramatic and erroneous extension of the absolute, non-statutory immunity available to private entities

that perform some form of regulatory role. By allowing an SRO to claim immunity regarding conduct that it exercises within its proprietary, non-regulatory sphere wherever that conduct is merely "incident to" its delegated regulatory functions, the Second Circuit's SRO immunity rule is contrary to the text of the Exchange Act, common law tradition, and this Court's own precedent.

This Court's review is also warranted because the Second Circuit's long-established rule conflicts with the law of three other circuits. This conflict is entrenched and incapable of resolution except by this Court, whose guidance is especially needed in this important area of law where lower courts have long searched for the proper boundaries of SRO immunity absent clear direction from the governing statute or this Court. Without this Court's review, uncertainty will persist over the extent to which the more than thirty SROs charged with overseeing aspects of major financial markets may evade accountability even for acts of intentional wrongdoing.

I. The Decision Below Is Contrary To The Text Of The Exchange Act, Traditional Immunity Doctrines At Common Law, And The Rationale Underlying Derivative Immunity.

No federal statute commands the expansive SRO immunity rule employed in the Second Circuit. Indeed, the text of the Exchange Act points decidedly against that approach. Neither is there a comparable immunity historically accorded at common law that Congress's silence can be read to preserve. Moreover, even if the court below was correct to ignore the

statutory text and historical tradition, and rely instead on the theory that private SROs enjoy an immunity derivative of the federal government's sovereign status, both this Court's prior decisions and principles of sound logic dictate that, at most, SROs should be derivatively immune for actions taken when actually performing functions delegated by the government.

A. The Plain Text Of The Exchange Act Forecloses The Expansive SRO Immunity Afforded By The Courts Below.

1. The proper starting point for evaluating a claim of absolute immunity is the statutory text Congress enacted. *See Hui v. Castaneda*, 130 S. Ct. 1845, 1850 (2010). Yet the Second Circuit's embrace of wholesale absolute immunity for all SRO conduct that is "incident to" the exercise of regulatory power cannot be squared with the text of the Exchange Act, 15 U.S.C. §§ 78a-78pp, the statute that creates the SROs and their rights and responsibilities in the first instance, *see* 15 U.S.C. §§ 78s, 78f, 78o-3, 78q-1. Put simply, no provision in the Exchange Act confers absolute immunity upon SROs for the scope of conduct recognized in the Second Circuit.

To the contrary, Congress considered whether to grant SROs immunity and did so in only two narrow and well-defined respects that are not applicable here. First, 15 U.S.C. § 78o-3(i)(4) states that registered securities associations (and exchanges reporting to such associations) "shall not have any liability to any person for any actions taken or omitted in good faith under" the subsection that

requires SROs to maintain registration and disciplinary data. Second, 15 U.S.C. § 78iii(b) declares that "[n]o self-regulatory organization shall have any liability to any person for any action taken or omitted in good faith pursuant to section 78eee(a)(1) and section 78eee(a)(2) of this title." Those provisions, in turn, require SROs to report when a member broker or dealer is approaching financial difficulty and authorize the SRO to provide assistance.

In three distinct ways, these provisions refute the Second Circuit's view that SRO's are properly awarded absolute immunity for conduct "incident to" their exercise of regulatory authority.

First, Congress's express textual provision of immunity in two limited circumstances would have been entirely unnecessary if Congress had also intended courts to immunize SROs for any conduct incident to the exercise of regulatory power. *See*, *e.g.*, *Pa. Dep't of Pub. Welfare v. Davenport*, 495 U.S. 552, 562 (1990) (noting that the Court has long "express[ed] a deep reluctance to interpret a statutory provision so as to render superfluous other provisions in the same enactment"); *cf. also Hercules Inc. v. United States*, 516 U.S. 417, 428-29 (1996) (refusing to recognize an implied indemnity claim where existing statutory language already confers indemnity "under specified circumstances"). It goes without saying, for example, that maintenance of disciplinary data is incident to an SRO's regulatory functions. If Congress had intended courts to immunize *all* "incident" activities, it would have had no reason to single out these few small areas of regulatory action for textual protection.

Second, while the statute provides immunity only for "good faith" SRO conduct, the Second Circuit provides absolute immunity for even intentional *bad faith* conduct, so long as it is incidental to a regulatory power. *See In re NYSE Specialists*, 503 F.3d at 98 (immunity turns "on whether specific acts and forbearances were incident to the exercise of regulatory power, and not on the propriety of those actions or inactions") (emphasis omitted). The Second Circuit thus has rendered superfluous both the textual provision of immunity for circumscribed conduct and Congress's express limitations on that immunity.

Third, where Congress has expressly provided immunity, it has done so only for conduct that is plainly an *actual* exercise of a delegated regulatory responsibility. For example, while passage of the bylaw amendments was necessary for the formation of the new consolidated SRO, which would then maintain disciplinary records and report financially troubled members to the Government, even respondent has not gone so far as to argue that this brings the "incident" proxy statement within the scope of the textual immunity provisions of the statute, 15 U.S.C. §§ 78o-3(i)(4), 78iii(b). That Congress limited textual immunity to actual regulatory conduct belies any suggestion it intended, but failed to mention, a broader immunity for actions merely incidental to the SROs' regulatory operations.

2. The Second Circuit found it "significant" that the SEC must approve amendment bylaws, Pet. App. 8a, suggesting that governmental oversight serves as an adequate substitute for private litigation over misconduct incident to SRO regulatory authority.

But that theory fails for reasons that are perfectly illustrated by this case. The SEC's Approval Order *expressly declined* to reach the merits of petitioner's state law fraud claims, and instead reserved that question for the courts, noting that question fell outside the agency's purview. *See* Exchange Act Release No. 56145A, 73 Fed. Reg. at 32377. Because the SEC will not regulate the truthfulness of proxy statements to SRO members, and because the Second Circuit has held such fraud immune from private litigation, the result is that *no one* can hold SROs accountable for even willful fraud in cases such as this.

That enforcement gap spans far more widely than fraudulent proxy statements. The Exchange Act limits the Government's authority over SROs to ensuring adequate performance of their actual delegated regulatory duties. For example, 15 U.S.C. §§ 78s(d)(1)-(2) authorize "appropriate regulatory agenc[ies]" to review SRO disciplinary sanctions, membership denials, and services. Similarly, 15 U.S.C. § 78s(h) gives regulatory agencies the power to suspend, censure and revoke the registration of an SRO only when the agency finds that the SRO has violated or failed to enforce the Exchange Act, other specifically enumerated federal securities laws and regulations, or the SRO's own rules.

Thus, federal agencies are powerless to oversee, enjoin, or punish SROs' wrongful *private* conduct that is merely "incident to" its regulatory authority. And as a result, there is no basis to expect that SEC review could fill the enforcement void created by the Second Circuit's expansive immunity rule. As a consequence, SROs are left unchecked to violate the

law without fear of private or governmental liability whenever they act within the vast no-man's land of private activities that happen to be "incident to" their regulatory powers – a wide swath of common activity that includes such conduct as the SROs' management of property, handling of financial accounts, provision of private services, internal organization, and collection of member dues.

B. The Second Circuit's SRO Immunity Rule Finds No Support In Historical Immunities Afforded At Common Law.

In some rare instances, even in the absence of a textual provision of immunity, this Court has assumed that Congress did not intend to displace well-known immunities that were deeply embedded in the law at the time the legislation was enacted. *See Butz v. Economou*, 438 U.S. 478, 508 (1978) (in cases involving claims of absolute immunity, the Court has "undertaken 'a considered inquiry into the immunity historically accorded the relevant official at common law and the interests behind it'") (quoting *Imbler v. Pachtman*, 424 U.S. 409, 421 (1977)); *Richardson v. McKnight,* 521 U.S. 399, 404 (1997) ("History does *not* reveal a 'firmly rooted' tradition of immunity applicable to privately employed prison guards."); *Owen v. City of Independence, Mo.*, 445 U.S. 622, 638 (1980) ("[T]here is no tradition of immunity for municipal corporations"); *Wyatt v. Cole*, 504 U.S. 158, 164-65 (1992) (no support in common law tradition for granting immunity to private parties who institute attachment proceedings under state replevin statutes).

In this case, however, history and the common law tradition offer no support for the immunity conferred by the Second Circuit.

1. Private, self-regulating securities exchanges have existed for over two centuries. As one commentator has written, "[s]ecurities industry self-regulation is about as old as the nation." Ernest E. Badway and Jonathan M. Busch, *Ending Securities Industry Self-Regulation As We Know It*, 57 RUTGERS L. REV. 1351, 1352 (2005). The New York Stock Exchange, for instance, was founded in 1792. *Id*. By 1934, when the Exchange Act was enacted, there were already at least twenty-one stock exchanges in existence, each of which was self-governed and self-regulated by "committees on business conduct, stock list, admission, arrangements, publicity, law, and arbitration." Marianne K. Smythe, *Government Supervised Self-Regulation in the Securities Industry and the Antitrust Laws: Suggestions for an Accommodation*, 62 N.C. L. REV. 475, 480 (1984).

Yet for roughly the first *two hundred years* of their existence, self-regulating securities organizations enjoyed no immunity from private suit. It was not until the 1980s that lower federal courts began holding SROs absolutely immune from private actions. *See, e.g.*, *Austin Mun. Sec., Inc. v. NASD, Inc.*, 757 F.2d 676, 697 (5th Cir. 1985). Thus, not until five decades after passage of the Securities Exchange Act, which formalized and strengthened the regulatory responsibilities that exchanges had long since taken on their own, did private SROs succeed in their first claim of immunity. And it was not until the early years of this century that the

Second Circuit expanded that immunity to cover "incidental" conduct.

Accordingly, there can be no claim that in 1934 Congress was aware of, and intended to retain, a common law immunity anything like the SRO immunity the Second Circuit enforced in this case.

2. As a striking point of contrast, at the time of the Exchange Act, there was a well-established common law tradition of extending absolute immunity to judicial and prosecutorial acts. *See, e.g.*, *Pierson v. Ray*, 386 U.S. 547, 554 (1967) (recognizing common law immunity for judges for "acts committed within their judicial jurisdiction"); *Bradley v. Fisher*, 80 U.S. (13 Wall.) 335 (1872) (same); *Butz*, 438 U.S. at 512 (judicial immunity extends to "quasi-judicial officers" in the executive branch); *Imbler*, 424 U.S. at 431 (prosecutors enjoy immunity when "initiating a prosecution and in presenting the State's case").

But even if that tradition could be extended to afford immunity to *private* entities such as the SROs, that extension would still fall well short of supporting the Second Circuit's expansive immunity rule. As this case illustrates, the Second Circuit has not limited immunity to cases involving SRO conduct akin to prosecution or adjudication. Issuing proxy solicitations is not a prosecutorial or judicial function under any stretch of the imagination.

Indeed, the Second Circuit's "incident to" immunity is far more encompassing than the immunity afforded to judges and prosecutors, who are immunized only when they actually perform the specific prosecutorial or adjudicative functions justifying the exceptional protection of absolute

immunity. *See*, *e.g.*, *Pierson*, 386 U.S. at 554 (judges enjoy absolute immunity only "for acts within the judicial role"); *Forrester v. White*, 484 U.S. 219, 227-28 (1988) (no judicial immunity for "administrative" as opposed to judicial decisions); *Harlow v. Fitzgerald*, 457 U.S. 800, 811 n.16 (1982) (acknowledging general rule that prosecutors do not enjoy absolute immunity for acts taken in their administrative or investigative capacities).

C. The Second Circuit's SRO Immunity Rule Is Not Supported By The Principle Of Derivative Sovereign Immunity.

Because SRO immunity is not rooted in the text of the Exchange Act or the common law tradition of judicial and prosecutorial immunity, some lower courts have suggested that private SROs should enjoy absolute immunity derivative of the federal government's sovereign status. That rationale, however, is decidedly inconsistent with the text and history discussed above, as well as the expansive immunity rule applied by the Second Circuit.

1. To begin with, this Court has not squarely addressed the issue of whether private entities like SROs may shield themselves from suit under the federal government's mantle of sovereign immunity simply because the government has granted them regulatory power. *See* Rohit A. Nafday, Comment, *From Sense to Nonsense and Back Again: SRO Immunity, Doctrinal Bait-and-Switch, and a Call for Coherence*, 77 U. CHI. L. REV. 847, 858 (2010) ("Congress has never indicated that SROs ought to enjoy sovereign immunity, nor, for that matter, has the Supreme Court."). And while the lower courts are

in general agreement that some form of derivative sovereign immunity ought to exist, they are in disarray over how that immunity should be applied in different contexts (yet another reason why this Court should grant review in this case). *See infra* 24-29.

Yet even assuming that the courts below are correct that private entities should enjoy some form of immunity derivative of their delegated governmental powers, that principle still fails to justify the Second Circuit's SRO immunity rule. The concept of derivative immunity is premised on the notion that immunity should track function and not form; that is, if a party engaged in a governmental regulatory function happens to be a private entity, it should be entitled to immunity just as the government would be itself. *See*, *e.g.*, *In re Series 7 Broker Qualification Exam Scoring Litig.*, 548 F.3d 110, 114-15 (D.C. Cir. 2008); *Weissman v. NASD*, 500 F.3d 1293, 1306 n.4 (11th Cir. 2007) (Tjoflat, J., dissenting).

Thus, under this theory of derivative immunity, SROs receive immunity because of *what they do*, not because of *who they are*. Derivative immunity is therefore appropriate – if at all – only when private SROs act in the stead of the federal government to perform functions that the government would otherwise perform. *Weissman*, 500 F.3d at 1297. But, as the Eleventh Circuit has explained, this rationale imposes its own limitation: "entities that enjoy absolute immunity when performing governmental functions cannot claim that immunity when they perform non-governmental functions." *Id.* at 1296.

The Second Circuit's approach, however, ignores this essential limitation. It extends immunity to SROs even when *what they do* is purely private business activity that is only incident to governmental power (such as soliciting votes from members for a bylaw amendment). In doing so, the Second Circuit altogether divorces its derivative immunity rule from the rule's rationale, leading to absurd results. Under the Second Circuit's approach, for example, an SRO could take out a $100 million loan to fund a new regulatory enforcement program and then refuse to pay back that loan when it comes due and argue that it is absolutely immune from suit over conduct "incident to" its regulatory power.

Worse still, what conduct is "incident" to regulatory power can be subject to an SRO's control and to potential manipulation. In this case, for example, NASD's proxy statement was deemed immunized because it was "incident to" a regulatory consolidation. Yet it was incident to that consolidation only because the SROs *themselves* had negotiated the bylaw change as a necessary closing condition so as to mollify the private demands of the larger NYSE member firms. Thus, if the Second Circuit is right, SROs can insulate even the most self-interested private conduct from liability through the nicety of deeming it a necessary condition to a regulatory change. For instance, if respondent and the NYSE had negotiated a closing condition requiring outlandish $100 million bonuses to be paid to each NASD executive through a bylaw amendment and then issued a blatantly fraudulent proxy statement declaring that the bonuses were required to comply with IRS regulations, the logic of the

Second Circuit's decision would compel dismissing a suit over that condition because the proxy statement was "incident to" the completion of the regulatory consolidation.

These results fly in the face of this Court's admonition that immunity must be based on a "discerning inquiry into whether the contributions of immunity to effective government in particular contexts outweigh the perhaps recurring harm to individual citizens." *Doe v. McMillan*, 412 U.S. 306, 320 (1973). When courts immunize purely private conduct that happens to be 'incident to' a regulatory function, the immunity contributes little (if anything) to effective government while exacting great harm on individual citizens who are left without recourse when the private SRO violates the law.

2. Two lines of this Court's decisions confirm the principle that private entities like SROs are immune (if at all) only when actually doing what the government has required them to do – and not for their own proprietary decisions, even if "incident to" their governmental functions.

a. First, the Second Circuit's rule is at odds with this Court's government contractor jurisprudence. Government contractors, like SROs, are retained to perform specific functions for the federal government. In *Boyle v. United Technologies Corp.*, 487 U.S. 500 (1988), this Court held that no liability would attach to a government contractor's actions when "(1) the United States approved reasonably precise specifications; [and] (2) the equipment conformed to those specifications . . . ." *Id.* at 512. On the other hand, the Court made clear that if a contractor's wrongful conduct was not required in order to comply

with the contract's specifications, immunity would be unavailable because liability would arise from the contractor's own decisions. *Id*. at 509.

Under *Boyle*, if NASD had been regulating its members pursuant to a contract with the SEC rather than a statutory delegation, it would have no immunity from petitioner's claims. The conduct giving rise to liability was not directed by the government – neither Congress nor the SEC required NASD and NYSE to merge their regulatory businesses; federal law did not require NASD to alter its voting rules; and needless to say, the government did not order NASD to lie to its members to secure approval for the bylaw amendments.

Thus, under *Boyle*, NASD would remain responsible for its own choices, even if those choices were incident to its contractual duties. There is no reason for a dramatically different rule when the delegation of governmental authority is accomplished by statute rather than by contract. Indeed, as discussed above, if anything, there is less reason to imply broad immunity when Congress has crafted the delegation itself and directly addressed the question of immunity.

b. The Second Circuit's rule is also incompatible with this Court's decisions on municipal liability. Municipal corporations, much like SROs, act as "private companies that carry out governmental functions." *Weissman*, 500 F.3d at 1297. At common law, and under 42 U.S.C. § 1983, when municipal corporations act "in their governmental capacity," they are afforded "complete immunity from civil responsibility." *Owen*, 445 U.S. at 645 n.27

(quotation marks omitted). By contrast, when municipal corporations are

> not acting in the exercise of their purely governmental functions, but are performing duties that pertain to the exercise of those private franchises, powers, and privileges which belong to them for their own corporate benefit, . . . then a different rule of liability is applied and they are generally held responsible for injuries arising from their negligent acts or their omissions . . . .

Id. (quoting W. Williams, *Liability of Municipal Corporations for Tort* § 4, at 9 (1901)).

This Court's municipal corporation immunity jurisprudence thus supports the same limit on SRO immunity as *Boyle*: no immunity extends to SRO actions that are not taken in a "governmental capacity" and that instead pertain to "private franchises, powers, and privileges" that further the private entity's "own corporate benefit" (such as the SRO's private management of its own funds, property, revenue-generating services, internal voting structure, and so on). *Owen*, 445 U.S. at 645 n.27 (citation omitted). The Second Circuit's rule, however, erroneously immunizes precisely this kind of private conduct so long as it is also "incident to" some regulatory power.

II. The Courts Of Appeals Are Divided Over The Scope Of Absolute Immunity To Which SROs Are Entitled.

Certiorari is also warranted because, as has been widely acknowledged, the circuits are divided over the test to apply in determining whether SRO

conduct is subject to absolute immunity. *See, e.g.*, Nafday, *supra*, at 848 (describing split among the circuits); Andrew J. Cavo, Note, Weissman v. National Association of Securities Dealers*: A Dangerously Narrow Interpretation of Absolute Immunity for Self-Regulatory Organizations*, 94 CORNELL L. REV. 415, 431 (2009) (same). While the Second Circuit insulates SRO wrongdoing from private suit whenever the SRO's conduct is "incident to" delegated regulatory authority, the Eleventh, Ninth, and D.C. Circuits hold that an SRO is entitled to absolute immunity only when it actually performs government-delegated regulatory, prosecutorial, and disciplinary functions. This conflict has existed and widened over the course of the last decade without any indication that it will be resolved unless this Court grants review. Because petitioner would prevail under the rule announced by other circuits, this case is an ideal vehicle through which to resolve the conflict.

1. As discussed, the Second Circuit has adopted an expansive rule that confers absolute immunity on an SRO not just when it exercises regulatory functions delegated to it by the government, but also whenever it acts "consistent with" or "incident to" delegated regulatory power. *In re NYSE Specialists Sec. Litig.*, 503 F.3d 89, 98 (2d Cir. 2007) (SROs are immune from suit over "acts and forbearances [that a]re *incident to* the exercise of regulatory power") (emphasis added); *DL Capital Group, LLC v. NASDAQ Stock Market, Inc.*, 409 F.3d 93, 96 (2d Cir. 2005) (An SRO is "entitled to immunity from suit when it engages in conduct *consistent with* the quasi-governmental powers delegated to it") (emphasis

added); *D'Alessio v. NYSE, Inc.* 258 F.3d 93, 106 (2d Cir. 2001) (same).[5]

In contrast, the Ninth, Eleventh, and D.C. Circuits afford SROs immunity only when they actually *perform* government-delegated prosecutorial, regulatory, or disciplinary functions. No immunity attaches in these circuits when the SRO engages in private activities, even if they are incident to or consistent with government-delegated power.

The Ninth Circuit was the first appeals court to adopt the narrower approach, beginning with its decision in *Sparta Surgical Corp. v. NASD, Inc.,* 159 F.3d 1209 (9th Cir. 1998). Recognizing that the "results of any immunity rule may be harsh," *id*. at 1215, the court held that "self-regulatory organizations do not enjoy complete immunity from suits; it is only when they are acting under the aegis of the Exchange Act's delegated authority that they so qualify. When conducting private business, [SROs] remain subject to liability," *id*. at 1214. *See also Partnership Exch. Sec. v. NASD*, 169 F.3d 606, 608 (9th Cir. 1999) (same); *Opulent Fund v. NASDAQ Stock Market, Inc.*, No. C-07-03683, 2007 WL 3010573 at *5 (N.D. Cal. Oct. 12, 2007) (rejecting SRO's claim to immunity under *Sparta* because

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[5] C*f. also PennMont Sec. v. Frucher*, 586 F.3d 242, 245 (3rd Cir. 2009) (noting district court holding that that "when a self-regulatory organization takes regulatory action *consistent with* the goals of the Exchange Act, the self regulatory organization is absolutely immune from private civil suits challenging the regulatory action," but resolving the case on other grounds) (emphasis added).

"calculat[ing] and disseminat[ing] an index price" was "non-regulatory" private business activity).

The Eleventh Circuit, sitting en banc, joined the Ninth Circuit's approach in *Weissman v. NASD, Inc.*, 500 F.3d 1293 (11th Cir. 2007). The plaintiff in that case had sued NASDAQ, a stock exchange then owned and operated by respondent NASD. In addition to regulating the exchange, NASDAQ had run a $100 million advertising campaign promoting, among other things, stock in WorldCom, shortly before that company's collapse. *Id*. at 1294. An investor who had purchased the stock sued, alleging that the advertising was fraudulent and misleading. On appeal, the Eleventh Circuit rejected NASDAQ's claim of immunity. The court held that "absolute immunity must be coterminous with an SRO's performance of a governmental function." *Id*. at 1297. Consequently, "[w]hen an SRO is not performing a purely regulatory, adjudicatory, or prosecutorial function, but rather acting in its own interest as a private entity, absolute immunity from suit ceases to obtain." *Id*.

The Eleventh Circuit expressly rejected the defendant's plea to adopt the Second Circuit's broader rule granting an SRO absolute immunity for "all activity that is 'consistent with' its powers and functions under the Exchange Act and SEC regulations." *Weissman*, 500 F.3d at 1297. It explained that "immunity is appropriate only when an SRO is performing regulatory, adjudicatory, or prosecutorial functions that would otherwise be performed by a government agency." *Id*.

Thus, the Eleventh Circuit ruled in the case before it that even if the advertisements were

incident to the NASDAQ's regulatory goals, the advertisements "were in no sense coterminous with the regulatory activity contemplated by the Exchange Act." *Weissman*, 500 F.3d at 1299. The court held instead that the challenged conduct was "private business activity, and '[w]hen conducting private business, [SROs] remain subject to liability.'" *Id*. (quoting *Sparta Surgical Corp.,* 159 F.3d at 1214).

One year later, the D.C. Circuit joined ranks in adopting the stricter SRO immunity rule. Like the Ninth and Eleventh Circuit, the D.C. Circuit held that SROs are entitled to immunity only when they "perform[] . . . regulatory, adjudicatory, or prosecutorial duties delegated by the SEC." *In re Series 7 Broker Qualification Exam Scoring Litig*., 548 F.3d 110, 114 (D.C. Cir. 2008) (citing *Weissman*, 500 F.3d at 198-99).[6]

2. Petitioner would have prevailed under the absolute immunity rule applied in the Eleventh, Ninth, and D.C. Circuits. The Second Circuit acknowledged that respondents' challenged conduct – "the proxy solicitation regarding amendments to the bylaws" – was only "incident to" the exercise of NASD's regulatory power. Pet. App. 7a. And because NASD's proxy statement furthered "its own

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[6] *Cf. also Zandford v. NASD, Inc.*, No. 94-7058, 1996 WL 135716, at *1 (D.C. Cir. 1998) (unpublished opinion) (holding that "[w]hile the NASD and DBCC disciplinary officers are entitled to absolute immunity for actions that are prosecutorial or adjudicative in nature, absolute immunity does not extend to acts that are purely investigatory or administrative") (internal citation omitted).

interest[s] as a private entity" – including its interests in increased member dues and bonuses for executives – as opposed to a "purely regulatory, adjudicatory, or prosecutorial function," *Weissman*, 500 F.3d at 1297, no absolute immunity would have attached in the Eleventh, Ninth, and D.C. Circuits.

3. Granting certiorari would also help to resolve other related conflicts in the law. The circuits are split over private entities' derivative immunity in a variety of contexts. *See, e.g.*, *Brooks v. Blue Cross & Blue Shield of Fla., Inc.*, 116 F.3d 1364, 1382 (11th Cir. 1997) (Medicare carrier enjoys derivative immunity unless it exceeds its "authority to act on the government's behalf"); *Pani v. Empire Blue Cross Blue Shield*, 152 F.3d 67, 72 (2d Cir. 1998) (private Medicare insurer immunized for actions that are "discretionary in nature and fall within the outer perimeter of the [entity's] duties"); *NF Indus., Inc. v. Export-Import Bank of U.S.*, 846 F.2d 998, 1001 (5th Cir. 1988) (private entity not entitled to immunity when it engages in "private business" instead of "governmental policymaking").

III. The Present Inconsistent Treatment Of SRO Claims Of Immunity Should Not Be Allowed To Persist Any Longer.

The present arbitrary disparate treatment of claims against SROs is intolerable. Without a uniform standard, SROs engaging in the same conduct in different jurisdictions presently face vastly different liability rules based solely on geographic happenstance. If the petitioner had been a corporate citizen of Florida and filed this suit in the Eleventh Circuit, it would have prevailed below.

This reality is not only unfair, but creates a substantial incentive for plaintiffs to engage in forum shopping: a plaintiff seeking to sue an SRO on behalf of a class of similarly situated businesses could simply seek a member residing in the Eleventh, Ninth, and D.C. Circuits to avoid facing the Second Circuit's more stringent rule.

There is no reason to delay the Court's intervention. The conflict among the circuits shows no signs of abatement. The Second Circuit has decided multiple cases dealing with SRO immunity and has unwaveringly affirmed its rule insulating SRO conduct wherever that conduct is "consistent with" or "incident to" regulatory power. Indeed, the Second Circuit applied that standard in this case despite the Eleventh Circuit's intervening decision in *Weissman*, which expressly rejected the Second Circuit's approach.

Neither can respondent credibly claim that the Eleventh, Ninth, and D.C. Circuits will all reverse themselves and begin applying the Second Circuit's rule. The Eleventh Circuit, sitting en banc, has already considered and refused to adopt that approach. Nor have the Ninth and D.C. circuits shown any indication that they are prepared to immunize more conduct than the SRO's actual performance of delegated regulatory, prosecutorial, and adjudicatory functions

That the Second Circuit's rule is entrenched, and incorrect, is especially significant given the outsized role that court plays in litigation regarding financial institutions. As the circuit having jurisdiction over New York City, a world financial center, the Second Circuit hears a lion's share of cases raising issues of

SRO immunity. Accordingly, further percolation is unlikely to yield any benefit.

IV. The Petition Presents Questions Of Recurring National Importance.

Certiorari is also warranted because the proper scope of SRO immunity is a question of great importance to the proper functioning of, and national confidence in, financial markets.

1. The SEC has registered more than thirty SROs in a diverse range of financial markets, including for stocks, futures, commodities, options, municipal bonds, over-the-counter derivatives, and others. *See* SECURITIES AND EXCHANGE COMMISSION, *Self-Regulatory Organization Rulemaking*, http://www.sec.gov/rules/sro.shtml. Many are private, for-profit institutions.[7]

As the U.S. Chamber of Commerce's Center for Capital Markets Competitiveness has explained, even as SRO influence over the markets "has grown dramatically over the past few decades," their "level

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[7] *See, e.g.*, Exchange Act Release No. 53721, 71 Fed. Reg. 26155, 23155 (April 25, 2006) (order approving conversion of the National Stock Exchange, an SRO, from a "nonprofit membership corporation to a Delaware for-profit stock corporation"); Exchange Act Release No. 51149, 70 Fed. Reg. 7531, 7531 (February 8, 2005) (order approving reorganization of the Chicago Stock Exchange, an SRO, from a non-profit corporation to a for-profit stock corporation); Exchange Act Release No. 49718, 69 Fed. Reg. 29611, 29611 (May 17, 2004) (order approving conversion of an SRO, the Pacific Exchange, from a "not-for-profit membership corporation" into a for-profit "stock corporation").

of accountability to their constituents has not kept pace." CENTER FOR CAPITAL MARKETS COMPETITIVENESS, U.S. CAPITAL MARKETS COMPETITIVENESS: THE UNFINISHED AGENDA 21 (2011). Because the SROs are "[u]nchallenged and largely unchecked, the influence of these organizations can be very detrimental to the development of vibrant capital markets." *Id*.

The SEC also has recognized that SROs are subject to significant conflicts of interest, operating both as government regulators and as private corporations with a wide array of independent institutional interests. Concept Release Concerning Self-Regulation, Release No. 34-50700 (Nov. 18, 2004).[8] The risk posed by that conflict has grown with heightened competition among SROs to increase the size of their membership and company listings. The SEC has further observed that the recent trend among many SROs to restructure as for-profit, shareholder-owned entities has introduced an even greater potential for "new conflicts of interest and issues of regulatory incentives." *Id*.

These divergent incentives – between what is best for the private SROs as businesses and what is best for effective regulation – are playing out today amidst a period of unrivaled turmoil in the financial markets. Confidence in the integrity and soundness of our financial institutions requires effective means for holding those institutions accountable for

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[8] *Available at* http://www.sec.gov/rules/concept/3450700.htm.

wrongdoing. That, in turn, requires certain and reasonable limitations on SRO immunity, both of which only this Court can provide.

2. Finally, in addition to posing a question of great practical importance, the petition raises issues of broader doctrinal significance that extend beyond the liability of financial market SROs.

SRO immunity is simply one form of a broader class of immunities that the lower courts have established for the benefit of private entities performing governmental functions in a range of settings, including with respect to Medicare,[9] farm credit,[10] and foreign banking.[11] In all of these contexts, the question arises whether, and to what extent, private entities that play a role in the administration of a federal program should be entitled to immunity from suit on a theory of derivative governmental immunity. Thus far, the Court has provided little guidance to lower courts

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[9] *See, e.g.*, *Pani*, 152 F.3d at 74-75 (Medicare carrier immune from private suit for performing investigatory functions delegated by federal statute); *Pine View Gardens, Inc. v. Mutual of Omaha Ins. Co.,* 485 F.2d 1073, 1074-75 (D.C. Cir. 1973) (claim for unpaid benefits against Medicare insurer barred by insurer's derivative sovereign immunity).

[10] *See, e.g.*, *Slotten v. Hoffman*, 999 F.2d 333, 336 (8th Cir. 1993) (private bank entitled to immunity when engaged in conduct required of it by Farm Credit Administration regulations).

[11] *See, e.g.*, *NF Indus., Inc. v. Export-Import Bank of U.S.*, 846 F.2d 998, 1001-02 (5th Cir. 1988) (private foreign credit association not entitled to derivative immunity where engaged in proprietary as opposed to governmental business).

struggling to balance the competing interests of encouraging private participation in governmental programs with the need for accountability and redress of unlawful conduct, consistent with the proper judicial role. This case provides the Court an opportunity to address this important and recurring issue.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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September 22, 2011

APPENDIX A

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Docket No. 10–945–cv

STANDARD INVESTMENT CHARTERED, INC., On behalf of itself and all others similarly situated,

Plaintiff-Appellant,

v.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INCORPORATED, aka NASD, NYSE Group, Inc., Mary L. Schapiro, Richard F. Brueckner, Babara Z. Sweeney, Financial Industry Regulatory Authority, Incorporated, T. Grant Callery, Todd Diganci And Howard M. Schloss,

Defendant-Appellees.

On Appeal from the United States District Court
for the Southern District of New York

(February 22, 2011)

Before: POOLER and HALL, Circuit Judges, COGAN, District Judge.[1]

PER CURIAM:

Appeal from an order of the United States District Court for the Southern District of New York (Rakoff, *J.*) granting Defendant–Appellees' Rule 12(b)(6) motion to dismiss. This case arises out of the consolidation of the National Association of Securities Dealers, Inc. ("NASD") with the regulatory arm of the New York Stock Exchange ("NYSE"), which resulted in the formation of the Financial Industry Regulatory Authority ("FINRA"). The district court held that Defendant–Appellees, which are self-regulatory organizations ("SROs"), and their officers were absolutely immune from private damages suits based upon alleged misstatements in a proxy solicitation that altered the bylaws of the NASD in connection with the creation of FINRA. As the district court explained, the bylaw amendments were incident to the regulatory function of the SROs insofar as they were a necessary prerequisite for consolidation, and amendment of the bylaws falls squarely within SRO statutory rulemaking authority as delegated by the SEC. We affirm.

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[1] Honorable Brian M. Cogan of the United States District Judge for the Eastern District of New York, sitting by designation.

BACKGROUND

Plaintiff–Appellant Standard Investment Chartered, Inc. ("Standard") is a California Corporation that was a member of the National Association of Securities Dealers Inc. ("NASD") at all times relevant to this lawsuit. Defendant–Appellees are the NASD and the former regulatory arm of the New York Stock Exchange ("NYSE")—the NYSE Group, Inc., as well as several NASD officers. NASD and NYSE Group, Inc. are SROs registered with the Securities and Exchange Commission ("SEC") as national securities associations pursuant to the Securities Exchange Act of 1934 ("Exchange Act").

The complaint alleges that NASD and its officers made misstatements in connection with a proxy solicitation in 2006 through which NASD sought to amend its bylaws to make them consonant with those of NYSE Group, Inc. so that the two entities could become one. Until NASD and NYSE Group, Inc. consolidated to form the Financial Industry Regulatory Authority, Inc. ("FINRA"), they each regulated separate markets, which meant, among other things, that the 170 broker-dealers belonging to both bodies were subject to two different sets of regulations that sometimes interacted in contradictory and confusing ways.

The consolidation was structured as an asset purchase agreement whereby NASD would acquire certain assets of NYSE Group, Inc. As a condition to closing, NASD was required to amend its bylaws, including by implementing a new voting regime—the NASD's "one member, one vote" system would be

replaced with a voting structure that distributed votes based upon the size of the member firm. The proxy solicitation also provided for a one-time "special member payment" of $35,000. Standard alleges that Defendant–Appellees misrepresented that $35,000 was the maximum possible payment that could be made.

On January 19, 2007, NASD's members voted in favor of the bylaw changes and the proposed amendments were sent to the SEC for approval, which is required by Section 19 of the Exchange Act and Rule 19b–4 promulgated thereunder. The SEC published the rules for public comment on March 20, 2007, *see* Exchange Act Release No. 55495, 90, SEC Docket No. 641 (Mar. 20, 2007), and ultimately approved them on July 26, 2007. Four days later, the consolidation became effective and FINRA was created.

Shortly before the SEC published the proposed bylaw changes for public comment, Standard commenced this lawsuit, which was dismissed on March 1, 2010, on the ground that Defendant–Appellees, as quasi-governmental organizations (and officers of such), were entitled to absolute immunity for their involvement in the proxy solicitation. The district court concluded that the proxy was incident to NASD's regulatory functions and otherwise issued in connection with powers delegated to NASD by the SEC.

We assume the parties' familiarity with the remaining facts, procedural history and issues presented for review.

DISCUSSION

I. Standard of Review

We review a district court's grant of a motion to dismiss de novo, accepting all factual allegations in the complaint as true and drawing all reasonable inferences in the plaintiff's favor. *Goldstein v. Pataki,* 516 F.3d 50, 56 (2d Cir.2008).

II. Legal Standard

There is no question that an SRO and its officers are entitled to absolute immunity from private damages suits in connection with the discharge of their regulatory responsibilities. *See DL Capital Group, LLC v. Nasdaq Stock Mkt., Inc.,* 409 F.3d 93, 96 (2d Cir.2005); *see also In re NYSE Specialists Sec. Litig.,* 503 F.3d 89, 96 (2d Cir.2007); *D'Alessio v. NYSE, Inc.,* 258 F.3d 93, 105 (2d Cir.2001); *Barbara v. NYSE,* 99 F.3d 49, 59 (2d Cir.1996); *accord Scher v. Nat'l Ass'n of Sec. Dealers, Inc.,* 218 Fed.Appx. 46, 47–48 (2d Cir.2007) (summary order). This immunity extends both to affirmative acts as well as to an SRO's omissions or failure to act. *See, e.g., NYSE Specialists,* 503 F.3d at 97 (failure to supervise); *Gurfein v. Ameritrade, Inc.,* 411 F.Supp.2d 416, 423 (S.D.N.Y.2006) (same); *Dexter v. DTC,* 406 F.Supp.2d 260, 263 (S.D.N.Y.2005) (setting of ex-dividend date); *Am. Benefits Group, Inc. v. Nat'l Ass'n of Sec. Dealers, Inc.,* No. 99 Civ. 4733, 1999 WL 605246, at *4 (S.D.N.Y. Aug. 10, 1999) (creation of reporting

requirements for companies included in the OTC Bulletin Board).

We have cautioned that the doctrine "is of a rare and exceptional character," *Barrett v. United States,* 798 F.2d 565, 571 (2d Cir.1986) (internal quotation marks omitted), and courts must examine the invocation of absolute immunity on a case by case basis, *DL Capital Group,* 409 F.3d at 97. The party asserting immunity bears the burden of demonstrating its entitlement. *D'Alessio,* 258 F.3d at 104. We apply a functional test to determine whether an SRO is entitled to immunity based upon the facts before us, *see NYSE Specialists,* 503 F.3d at 96, which requires us to look at "the nature of the function performed, not the identity of the actor who performed it," *Forrester v. White,* 484 U.S. 219, 229, 108 S.Ct. 538, 98 L.Ed.2d 555 (1988).

As we recognized in *NYSE Specialists,* we have found stock exchange SROs absolutely immune from suit where the alleged misconduct concerned (1) disciplinary proceedings against exchange members, *Barbara,* 99 F.3d at 59; (2) the enforcement of security rules and regulations and general regulatory oversight over exchange members, *D'Alessio,* 258 F.3d at 106; (3) the interpretation of the securities laws and regulations as applied to the exchange or its members, *id*.; (4) the referral of exchange members to the SEC and other government agencies for civil enforcement or criminal prosecution under the securities laws, *id*.; and (5) the public announcement of regulatory decisions, *DL Capital Group,* 409 F.3d at 98. Today, we add to that list an SRO's

amendment of its bylaws where, as here, the amendments are inextricable from the SRO's role as a regulator.

As the district court observed in this case, "[i]t is patent that the consolidation that transferred NASD's and NYSE's regulatory powers to the resulting FINRA is, on its face, an exercise of the SRO's delegated regulatory functions and thus entitled to absolute immunity." *Standard Inv. Chartered, Inc. v. Nat'l Ass'n of Sec. Dealers, Inc.,* Nos. 07 Civ.2014, 08 Civ. 11193, 2010 WL 749844, at *1 (S.D.N.Y. Mar. 1, 2010). The question confronting the court, however, was whether the proxy solicitation regarding amendments to the bylaws, which was incident to the consolidation, also constituted an exercise of NASD's regulatory function. On this point, the district court explained that, "[a]lthough the shareholder vote for which the proxy statement was issued did not constitute a vote on the regulatory consolidation itself, the approval of the by-law amendments was not only a necessary prerequisite to the completion of that consolidation, but also was promoted as such in the proxy itself." *Id.* The district court further noted that "amendment of the by-laws itself falls within the parameters of NASD's statutory rule-making authority." *Id.* (citing 15 U.S.C. §§ 78s(b), 78c(a)(27)). Accordingly, as the district court correctly concluded, the proxy solicitation, which was the only vehicle available to NASD for amending its bylaws, was plainly "incident to the exercise of regulatory power," *see NYSE Specialists,* 503 F.3d at 98, and therefore an activity to which immunity attached.

We also believe that it is significant that NASD cannot alter its bylaws without approval from the SEC, that the SEC is authorized to develop its own procedure for receiving input on new rules from those affected by any proposed changes, *see* 15 U.S.C. § 78s(b)(1) (requiring SROs to file proposed rule changes with the SEC in accordance with such rules as the SEC may prescribe and outlining the notice and comment period), and that the SEC retains discretion to amend the rules of any SRO, *see* 15 U.S.C. § 78s(c). The statutory and regulatory framework highlights to us the extent to which an SRO's bylaws are intimately intertwined with the regulatory powers delegated to SROs by the SEC and underscore our conviction that immunity attaches to the proxy solicitation here.

We have considered Appellant's remaining arguments and conclude that they are without merit.

CONCLUSION

For the reasons stated herein, we **AFFIRM** the judgment of the district court.

APPENDIX B

UNITED STATES DISTRICT COURT,
S.D. NEW YORK

STANDARD INVESTMENT CHARTERED, INC.,

Plaintiff,

v.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. et al.,

Defendants.

Benchmark Financial Services, Inc.,

Plaintiff,

v.

Financial Industry Regulatory Authority, Inc. et al.,

Defendants.

Nos. 07 Civ.2014(JSR), 08 Civ. 11193(JSR).

March 1, 2010.

MEMORANDUM ORDER

JED S. RAKOFF, District Judge.

These two related cases arise out of the regulatory consolidation, in 2007, of two self-regulatory organizations ("SROs")—the National Association of Securities Dealers, Inc. ("NASD") and the regulatory arm of the New York Stock Exchange ("NYSE")—to form the Financial Industry Regulatory Authority, Inc. ("FINRA"), the sole private regulator of member firms. Plaintiffs, who were members of NASD at the time of the consolidation, allege that material misrepresentations were made in the proxy statement that solicited NASD shareholder votes in favor of certain by—law amendments that were a necessary prerequisite to the consolidation. Most particularly, plaintiffs allege that the proxy statement falsely asserted that $35,000 was the maximum amount that NASD, a not—for—profit entity, was authorized by the Internal Revenue Service to pay members in connection with the merger.

While these cases were still pending before the late Honorable Shirley Wohl Kram, to whom they were originally assigned, defendants filed a motion to dismiss in the *Benchmark* action. Subsequent to the reassignment, the defendants in the *Standard* action filed motions to dismiss, and this Court received full briefing on all the motions and then heard oral argument on December 16, 2009. Among many reasons argued by defendants for dismissing the claims, one looms particularly large: defendants claim that they are entitled to absolute immunity. *See Barbara v. New York Stock Exchange, Inc.,* 99

F.3d 49, 59 (2d Cir.1996). Because the Court agrees, and on this ground dismisses the complaints, the Court does not reach the defendants' other arguments.

Pursuant to the Securities Exchange Act of 1934, 15 U.S.C. §§ 78a—78oo, the United States Securities and Exchange Commission is authorized to delegate certain regulatory functions to SROs, which are therefore considered "quasi—governmental" bodies. *PL Capital Group, LLC v. Nasdaq Stock Market, Inc.,* 409 F.3d 93, 95 (2d Cir.2005). As a result, SROs and their officers are absolutely immune from private damages suits challenging official conduct performed within the scope of their regulatory functions. *See, e.g., PL Capital Group,* 409 F.3d at 94–97. This immunity, being absolute, turns "on whether specific acts and forbearances were incident to the exercise of regulatory power, and not on the propriety of those actions or inactions." *In re NYSE Specialists S.E.C. Litig.,* 503 F.3d 89, 98 (2d Cir.2007).

It is patent that the consolidation that transferred NASD's and NYSE's regulatory powers to the resulting FINRA is, on its face, an exercise of the SROs' delegated regulatory functions and thus entitled to absolute immunity. However, plaintiffs contend that the actions they are challenging—that is, the making of the alleged misstatements in the proxy statement—pertain solely to the proprietary functions of the SROs, to which absolute immunity does not apply. In particular, they argue that the alleged misstatement about the $35,000 limit on payment related to defendants' finances, not their

regulatory functions. But this attempt to parse the proxy in order to separate "financially–related" statements from "regulatory–related" statements is artificial and unconvincing. Although the shareholder vote for which the proxy statement was issued did not constitute a vote on the regulatory consolidation itself, the approval of the by-law amendments was not only a necessary prerequisite to the completion of that consolidation, but also was promoted as such in the proxy itself. *See, e.g.,* Proxy Statement at 8 (Dec. 14, 2006) ("The Board of Governors has the authority to approve the Transaction and members are being asked only to approve the amendments to the NASD By–Laws. However, one of the conditions to the closing of the Transaction is member approval of the amendments to the By–Laws."). Moreover, amendment of the by–laws itself falls within the parameters of NASD's statutory rulemaking authority. *See* 15 U.S.C. § 78s(b); *id.* § 78c(a)(27). To focus on the fact that amendment to the by–laws also encompassed a financial component would be to miss the entire purpose of the reorganization–a regulatory purpose to which immunity applies. *See, e.g., D'Alessio v. New York Stock Exchange, Inc.,* 258 F.3d 93, 98, 105–06 (2d Cir.2001); *Dexter v. Depository Trust & Clearing Corp.,* 406 F.Supp.2d 260, 263–64 (S.D.N.Y.2005), *aff'd,* 219 F. App'x 91 (2d Cir.2007).

Accordingly, because all the defendants are entitled to absolute immunity, the Court hereby grants the defendants' motions to dismiss and dismisses both actions with prejudice.

SO ORDERED.

APPENDIX C

Release No. 56145A (S.E.C. Release No.), Release No. 34-56145A (S.E.C. Release No.), 93 S.E.C. Docket 986 (S.E.C. Release No.), 2008 WL 2677219 (S.E.C. Release No.)

S.E.C. Release No.
Securities Exchange Act of 1934

SECURITIES AND EXCHANGE COMMISSION
(S.E.C.)

SELF-REGULATORY ORGANIZATIONS; NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC. (N/K/A FINANCIAL INDUSTRY REGULATORY AUTHORITY, INC.); ORDER APPROVING PROPOSED RULE CHANGE TO AMEND THE BY-LAWS OF NASD TO IMPLEMENT GOVERNANCE AND RELATED CHANGES TO ACCOMMODATE THE CONSOLIDATION OF THE MEMBER FIRM REGULATORY FUNCTIONS OF NASD AND NYSE REGULATION, INC.

File No. SR-NASD-2007-023
May 30, 2008

Amended

In Part V of Securities Exchange Act Release No. 56145 ("Release No. 34-56145"), issued July 26,

2007,[2] the Securities and Exchange Commission ("Commission") is adding, immediately after the following sentence:

> "Accordingly, after reviewing the record in this matter, the Commission believes that NASD has provided sufficient basis on which the Commission can find that, under the Exchange Act, NASD complied with its Certificate of Incorporation and By-Laws with respect to the proxy approval process and that the proposed amendments to its By-Laws were properly approved by NASD members."

the following paragraph:

> "This finding as to NASD compliance and members' approval is not a definitive adjudication under state law, such as a trial court would make after an evidentiary hearing, regarding the claim that the proxy statement was misleading. Except to the extent that state law informs the Commission's finding that, as a federal matter under the Exchange Act, NASD complied with its Certificate of Incorporation and By-Laws with respect to the proxy approval process and that the proposed amendments to its By-Laws were properly approved by NASD members, the Commission is not purporting to decide a question of state law. The Commission does

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[2] See Securities Exchange Act Release No. 56145 (July 26, 2007), 72 FR 42169 (August 1, 2007) (FR Doc. E7-14855).

> not intend that its determination regarding the NASD's uncontradicted prima facie showing before the Commission that the proxy statement was not misleading be binding on a court in a claim based on state law."

In adding this clarifying language, the Commission is not vacating, nullifying or rendering void Release No. 34-56145, which approved NASD's proposed rule change to amend the By-Laws of NASD to implement governance and related changes to accommodate the consolidation of the member firm regulatory functions of NASD and NYSE Regulation, Inc. Release No. 34-56145, as amended herein, remains in effect as of July 26, 2007, the date it was issued by the Commission.

By the Commission.
Florence E. Harmon
Acting Secretary

APPENDIX D

UNITED STATES COURT OF APPEALS
FOR THE
SECOND CIRCUIT

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the Daniel Patrick Moynihan United States Courthouse, 500 Pearl Street, in the City of New York, on the 25th day of April, two thousand eleven,

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ORDER

Docket No : 10-945

Standard Investment Chartered, Incorporated, On behalf of itself and all others similarly situated,

Plaintiff - Appellant,

v.

National Association of Securities Dealers, Incorporated, AKA NASD, NYSE Group,Inc., Mary L. Schapiro, Richard F. Brueckner, Barbara Z. Sweeney, Financial Industry Regulatory Authority Incorporated, T. Grant Callery, Todd Diganci, Howard M. Schloss,

Defendants - Appellees.

Appellant Standard Investment Chartered, Incorporated, filed a petition for panel rehearing, or, in the alternative, for rehearing en banc. The panel that determined the appeal has considered the request for panel rehearing, and the active members of the Court have considered the request for rehearing en banc.

IT IS HEREBY ORDERED that the petition is denied.

For the Court:

Catherine O'Hagan Wolfe, Clerk

[SEAL]

/s/ *Catherine O'Hagan Wolfe*

APPENDIX E

RELEVANT STATUTORY PROVISIONS

15 U.S.C. § 78s.

§ 78s. Registration, responsibilities, and oversight of self-regulatory organizations

(a) Registration procedures; notice of filing; other regulatory agencies

(1) The Commission shall, upon the filing of an application for registration as a national securities exchange, registered securities association, or registered clearing agency, pursuant to section 78f, 78*o*-3, or 78q-1 of this title, respectively, publish notice of such filing and afford interested persons an opportunity to submit written data, views, and arguments concerning such application. Within ninety days of the date of publication of such notice (or within such longer period as to which the applicant consents), the Commission shall--

(A) by order grant such registration, or

(B) institute proceedings to determine whether registration should be denied. Such proceedings shall include notice of the grounds for denial under consideration and opportunity for hearing and shall be concluded within one hundred eighty days of the date of a publication of notice of the filing of the application for registration. At the

conclusion of such proceedings the Commission, by order, shall grant or deny such registration. The Commission may extend the time for conclusion of such proceedings for up to ninety days if it finds good cause for such extension and publishes its reasons for so finding or for such longer period as to which the applicant consents.

The Commission shall grant such registration if it finds that the requirements of this chapter and the rules and regulations thereunder with respect to the applicant are satisfied. The Commission shall deny such registration if it does not make such finding. . . .

(b) Proposed rule changes; notice; proceedings

(1) Each self-regulatory organization shall file with the Commission, in accordance with such rules as the Commission may prescribe, copies of any proposed rule or any proposed change in, addition to, or deletion from the rules of such self-regulatory organization (hereinafter in this subsection collectively referred to as a "proposed rule change") accompanied by a concise general statement of the basis and purpose of such proposed rule change. The Commission shall, as soon as practicable after the date of the filing of any proposed rule change, publish notice thereof together with the terms of substance of the proposed rule change or a description of the subjects and issues involved. The Commission

shall give interested persons an opportunity to submit written data, views, and arguments concerning such proposed rule change. No proposed rule change shall take effect unless approved by the Commission or otherwise permitted in accordance with the provisions of this subsection. . . .

(2) Approval process

. . . .

(C) Standards for approval and disapproval

(i) Approval

The Commission shall approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of this chapter and the rules and regulations issued under this chapter that are applicable to such organization.

(ii) Disapproval

The Commission shall disapprove a proposed rule change of a self-regulatory organization if it does not make a finding described in clause (i). . . .

(d) Notice of disciplinary action taken by self-regulatory organization against a member or participant; review of action by appropriate regulatory agency; procedure

(1) If any self-regulatory organization imposes any final disciplinary sanction on any member thereof or participant therein, denies membership or participation to any applicant, or prohibits or limits any person in respect to access to services offered by such organization or member thereof or if any self-regulatory organization (other than a registered clearing agency) imposes any final disciplinary sanction on any person associated with a member or bars any person from becoming associated with a member, the self-regulatory organization shall promptly file notice thereof with the appropriate regulatory agency for the self-regulatory organization and (if other than the appropriate regulatory agency for the self-regulatory organization) the appropriate regulatory agency for such member, participant, applicant, or other person. The notice shall be in such form and contain such information as the appropriate regulatory agency for the self-regulatory organization, by rule, may prescribe as necessary or appropriate in furtherance of the purposes of this chapter.

(2) Any action with respect to which a self-regulatory organization is required by paragraph (1) of this subsection to file notice shall be subject to review by the appropriate regulatory agency

for such member, participant, applicant, or other person, on its own motion, or upon application by any person aggrieved thereby filed within thirty days after the date such notice was filed with such appropriate regulatory agency and received by such aggrieved person, or within such longer period as such appropriate regulatory agency may determine. Application to such appropriate regulatory agency for review, or the institution of review by such appropriate regulatory agency on its own motion, shall not operate as a stay of such action unless such appropriate regulatory agency otherwise orders, summarily or after notice and opportunity for hearing on the question of a stay (which hearing may consist solely of the submission of affidavits or presentation of oral arguments). Each appropriate regulatory agency shall establish for appropriate cases an expedited procedure for consideration and determination of the question of a stay. . . .

(h) Suspension or revocation of self-regulatory organization's registration; censure; other sanctions

(1) The appropriate regulatory agency for a self-regulatory organization is authorized, by order, if in its opinion such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, to suspend for a period not exceeding twelve months or revoke the registration of such self-regulatory

organization, or to censure or impose limitations upon the activities, functions, and operations of such self-regulatory organization, if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such self-regulatory organization has violated or is unable to comply with any provision of this chapter, the rules or regulations thereunder, or its own rules or without reasonable justification or excuse has failed to enforce compliance--

(A) in the case of a national securities exchange, with any such provision by a member thereof or a person associated with a member thereof;

(B) in the case of a registered securities association, with any such provision or any provision of the rules of the Municipal Securities Rulemaking Board by a member thereof or a person associated with a member thereof; or

(C) in the case of a registered clearing agency, with any provision of its own rules by a participant therein.

(2) The appropriate regulatory agency for a self-regulatory organization is authorized, by order, if in its opinion such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, to suspend for a period not exceeding twelve months or expel from such self-regulatory organization

any member thereof or participant therein, if such member or participant is subject to an order of the Commission pursuant to section 78*o*(b)(4) of this title or if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such member or participant has willfully violated or has effected any transaction for any other person who, such member or participant had reason to believe, was violating with respect to such transaction--

(A) in the case of a national securities exchange, any provision of the Securities Act of 1933 [15 U.S.C.A. § 77a et seq.], the Investment Advisers Act of 1940 [15 U.S.C.A. § 80b-1 et seq.], the Investment Company Act of 1940 [15 U.S.C.A. § 80a-1 et seq.], this chapter, or the rules or regulations under any of such statutes;

(B) in the case of a registered securities association, any provision of the Securities Act of 1933, the Investment Advisers Act of 1940, the Investment Company Act of 1940, this chapter, the rules or regulations under any of such statutes, or the rules of the Municipal Securities Rulemaking Board; or

(C) in the case of a registered clearing agency, any provision of the rules of the clearing agency.

(3) The appropriate regulatory agency for a national securities exchange or registered securities association is authorized, by order, if in its opinion such action is necessary or

appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, to suspend for a period not exceeding twelve months or to bar any person from being associated with a member of such national securities exchange or registered securities association, if such person is subject to an order of the Commission pursuant to section 78*o*(b)(6) of this title or if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such person has willfully violated or has effected any transaction for any other person who, such person associated with a member had reason to believe, was violating with respect to such transaction--

(A) in the case of a national securities exchange, any provision of the Securities Act of 1933, the Investment Advisers Act of 1940, the Investment Company Act of 1940, this chapter, or the rules or regulations under any of such statutes; or

(B) in the case of a registered securities association, any provision of the Securities Act of 1933, the Investment Advisers Act of 1940, the Investment Company Act of 1940, this chapter, the rules or regulations under any of the statutes, or the rules of the Municipal Securities Rulemaking Board.

(4) The appropriate regulatory agency for a self-regulatory organization is authorized, by order, if in its opinion such action is necessary or

appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this chapter, to remove from office or censure any person who is, or at the time of the alleged misconduct was, an officer or director of such self-regulatory organization, if such appropriate regulatory agency finds, on the record after notice and opportunity for hearing, that such person has willfully violated any provision of this chapter, the rules or regulations thereunder, or the rules of such self-regulatory organization, willfully abused his authority, or without reasonable justification or excuse has failed to enforce compliance--

(A) in the case of a national securities exchange, with any such provision by any member or person associated with a member;

(B) in the case of a registered securities association, with any such provision or any provision of the rules of the Municipal Securities Rulemaking Board by any member or person associated with a member; or

(C) in the case of a registered clearing agency, with any provision of the rules of the clearing agency by any participant. . . .

15 U.S.C § 78o-3

§ 78*o*-3. Registered securities associations

. . .

(i) Obligation to maintain registration, disciplinary, and other data

(1) Maintenance of system to respond to inquiries

A registered securities association shall--

(A) establish and maintain a system for collecting and retaining registration information;

(B) establish and maintain a toll-free telephone listing, and a readily accessible electronic or other process, to receive and promptly respond to inquiries regarding--

(i) registration information on its members and their associated persons; and

(ii) registration information on the members and their associated persons of any registered national securities exchange that uses the system described in subparagraph (A) for the registration of its members and their associated persons; and

(C) adopt rules governing the process for making inquiries and the type, scope, and presentation of information to be provided in response to such inquiries in consultation with any registered national securities exchange providing information pursuant to subparagraph (B)(ii).

(2) Recovery of costs

A registered securities association may charge persons making inquiries described in paragraph (1)(B), other than individual investors, reasonable fees for responses to such inquiries.

(3) Process for disputed information

Each registered securities association shall adopt rules establishing an administrative process for disputing the accuracy of information provided in response to inquiries under this subsection in consultation with any registered national securities exchange providing information pursuant to paragraph (1)(B)(ii).

(4) Limitation on liability

A registered securities association, or an exchange reporting information to such an association, shall not have any liability to any person for any actions taken or omitted in good faith under this subsection.

(5) Definition

For purposes of this subsection, the term "registration information" means the information reported in connection with the registration or licensing of brokers and dealers and their

associated persons, including disciplinary actions, regulatory, judicial, and arbitration proceedings, and other information required by law, or exchange or association rule, and the source and status of such information.

15 U.S.C. § 78iii(b)

§ 78iii. Functions of self-regulatory organizations

(a) Collection agent

Each self-regulatory organization shall act as collection agent for SIPC to collect the assessments payable by all members of SIPC for whom such self-regulatory organization is the examining authority, unless SIPC designates a self-regulatory organization other than the examining authority to act as collection agent for any member of SIPC who is a member of or participant in more than one self-regulatory organization. If the only self-regulatory organization of which a member of SIPC is a member or in which it is a participant is a registered clearing agency that is not the examining authority for the member, SIPC may, nevertheless, designate such registered clearing agency as collection agent for the member or may require that payments be made directly to SIPC. The collection agent shall be obligated to remit to SIPC assessments made under section 78ddd of this title only to the extent that payments of such assessment are received by such collection agent. Members of SIPC who are not members of or participants in a self-regulatory organization shall make payments directly to SIPC.

(b) Immunity

No self-regulatory organization shall have any liability to any person for any action taken or omitted in good faith pursuant to section 78eee(a)(1) and section 78eee(a)(2) of this title.

(c) Inspections

The self-regulatory organization of which a member of SIPC is a member or in which it is a participant shall inspect or examine such member for compliance with applicable financial responsibility rules, except that--

(1) if the self-regulatory organization is a registered clearing agency, the Commission may designate itself as responsible for the examination of such member for compliance with applicable financial responsibility rules; and

(2) if a member of SIPC is a member of or participant in more than one self-regulatory organization, the Commission, pursuant to section 78q(d) of this title, shall designate one of such self-regulatory organizations or itself as responsible for the examination of such member for compliance with applicable financial responsibility rules.

(d) Reports

There shall be filed with SIPC by the self-regulatory organizations such reports of inspections or examinations of the members of SIPC (or copies thereof) as may be designated by SIPC by bylaw or rule.

(e) Consultation

SIPC shall consult and cooperate with the self-regulatory organizations toward the end:

(1) that there may be developed and carried into effect procedures reasonably designed to detect

approaching financial difficulty upon the part of any member of SIPC;

(2) that, as nearly as may be practicable, examinations to ascertain whether members of SIPC are in compliance with applicable financial responsibility rules will be conducted by the self-regulatory organizations under appropriate standards (both as to method and scope) and reports of such examinations will, where appropriate, be standard in form; and

(3) that, as frequently as may be practicable under the circumstances, each member of SIPC will file financial information with, and be examined by, the self-regulatory organization which is the examining authority for such member.

(f) Financial condition of members

The Commission may, by such rules as it determines necessary or appropriate in the public interest and to carry out the purposes of this chapter, require any self-regulatory organization to furnish SIPC with reports and records (or copies thereof) relating to the financial condition of members of or participants in such self-regulatory organization.

15 U.S.C. § 78eee

§ 78eee. Protection of customers

(a) Determination of need of protection

(1) Notice to SIPC

If the Commission or any self-regulatory organization is aware of facts which lead it to believe that any broker or dealer subject to its regulation is in or is approaching financial difficulty, it shall immediately notify SIPC, and, if such notification is by a self-regulatory organization, the Commission.

(2) Action by self-regulatory organization

If a self-regulatory organization has given notice to SIPC pursuant to subsection (a)(1) of this section with respect to a broker or dealer, and such broker or dealer undertakes to liquidate or reduce its business either pursuant to the direction of a self-regulatory organization or voluntarily, such self-regulatory organization may render such assistance or oversight to such broker or dealer as it considers appropriate to protect the interests of customers of such broker or dealer. The assistance or oversight by a self-regulatory organization shall not be deemed the assumption or adoption by such self-regulatory organization of any obligation or liability to customers, other creditors, shareholders, or partners of the broker or dealer, and shall not prevent or act as a bar to any action by SIPC. . . .