

and one or more short index futures traded on a board of trade or one or more standardized options contracts as defined in § 240.9b-1(a)(4) of this chapter, persons need not aggregate the long stock position with short stock positions in other proprietary accounts provided that:

(1) The short stock positions have been created and maintained in the course of bona fide arbitrage, risk arbitrage, or bona fide hedge activities; and

(2) The sale does not occur during a period commencing at the time that the Dow Jones Industrial Average has declined by two percent or more from its closing value on the previous day and terminating upon the establishment of the closing value of the Dow Jones Industrial Average on the next succeeding trading day.

§ 242.201 Price test and marking requirements

(a) Definitions. For the purposes of this section:

(1) The term *actively traded security* shall have the same meaning as in § 242.101(c)(1).

(2) The term *average daily trading volume* shall have the same meaning as in § 242.100(b).

(3) The term *consolidated best bid and offer* shall have the same meaning as in § 240.11Ac1-5(a)(7) of this chapter.

(4) The term *covered security* shall mean all national market system securities as defined in § 240.11Aa2-1 of this chapter, but shall exclude Nasdaq Small Cap securities, as determined by NASD rules.

(5) The term *odd lot* shall mean an order for the purchase or sale of a covered security in an amount less than a round lot.

(6) The term *responsible broker or dealer* shall have the same meaning as in § 240.11Ac1-1(a)(21) of this chapter.

(7) The term *riskless principal* shall mean a transaction in which a broker or dealer after having received an order to sell a security, sells the security as principal at the same price to satisfy the order to sell. The sell order must be given the same per-share price at which the broker or dealer sold shares to satisfy the facilitated order, exclusive of any explicitly disclosed markup or markdown, commission equivalent or other fee. In addition, for purposes of this section, a broker or dealer must have written policies and procedures in place to assure that, at a minimum: the customer order was received prior to the offsetting transaction; the offsetting transaction is allocated to a riskless principal or customer account within 60

seconds of execution; the broker or dealer has supervisory systems in place to produce records that enable the broker or dealer to accurately and readily reconstruct, in a time-sequenced manner, all orders which a broker or dealer relies pursuant to this exception.

(b) All short sales of any covered security must be effected at a price at least one cent above the current best bid displayed as part of the consolidated best bid and offer at the time of execution.

(c) A broker or dealer must mark all sell orders of any security as either "long," "short," or "short exempt." A broker or dealer shall mark an order to sell a security "long" only if the seller owns the security being sold and either:

(1) The security to be delivered is in the physical possession or control of the broker or dealer; or

(2) The security will be in the physical possession or control of the broker or dealer no later than the settlement of the transaction. An order shall be marked "short exempt" if the sale is effected pursuant to one of the exceptions in paragraph (d) of this section.

(d) The provisions of paragraph (b) of this section shall not apply to:

(1) Any sale by any person of a covered security, for an account in which he has an interest, if such person owns the security and intends to deliver such security as soon as is possible without undue inconvenience or expense;

(2) Any sale by a broker or dealer of a covered security for an account in which it has no interest, pursuant to an order marked long;

(3) Any sale of a covered security by a market maker to off-set customer odd-lot orders or to liquidate an odd-lot position by a single round lot sell order which changes such broker or dealer's position by no more than a unit of trading;

(4) Any sale of a covered security by a responsible broker or dealer effected at a price equal to the consolidated best offer when the market for the covered security is locked or crossed, provided however, that the exception shall not apply to any broker or dealer who initiated the locked or crossed market;

(5) Any sale of a covered security for a special arbitrage account by a person who is presently entitled to acquire another security, provided that the security sold short is in the same class as the security he is entitled to acquire, the short sale is in an amount equivalent to the number of the securities that he is entitled to acquire, the sale is effected to profit from a current price difference between the security sold short and the

security he is entitled to acquire, and the person subsequently acquires or purchases the security upon which the short sale was based. A person shall be deemed entitled to acquire a security if:

(i) He has an unconditional right or option to acquire or purchase the security at a specific price and in a specific amount when the short sale is effected; and

(ii) The right of acquisition was originally attached to or represented by another security, or was issued to all holders of the securities;

(6) Any sale of a covered security for a special international arbitrage account effected to profit from a current price difference between a security on a foreign securities market and a security on a securities market subject to the jurisdiction of the United States, provided that the short seller has an offer to buy on a foreign market that allows him to immediately cover the short sale at the time it was made. For the purposes of this section, a depositary receipt of a security shall be deemed to be the same security as the security represented by such receipt;

(7)(i) Any sale of a covered security by an underwriter or member of a syndicate or group participating in the distribution of a security in connection with an over-allotment of securities; or

(ii) Any lay-off sale by an underwriter or member of a syndicate or group in connection with a distribution of securities through rights or a standby underwriting commitment;

(8) Any sale of a covered security at the volume weighted average price (VWAP) that meets the following criteria:

(i) The sale is entered into and matched before the regular trading session opens and the execution price of the VWAP matched trade will be determined after the close of the regular trading session; and

(ii) The VWAP for the covered security is calculated by:

(A) Calculating the values for every regular way trade reported in the consolidated system, or on a primary market that accounts for seventy-five percent or more of the covered security's average daily trading volume for the security during the regular trading session, by multiplying each such price by the total number of shares traded at that price;

(B) Compiling an aggregate sum of all values; and

(C) Dividing the aggregate sum by the total number of reported shares for that day in the security; and

(iii) The transactions are reported using a special VWAP trade modifier; and