

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-66819; File No. SR-FINRA-2011-058)

April 17, 2012

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 to Proposed Rule Change to Amend FINRA Rule 6433 (Minimum Quotation Size Requirements for OTC Equity Securities)

I. Introduction

On October 6, 2011, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend FINRA Rule 6433 (Minimum Quotation Size Requirements for OTC Equity Securities). The proposed rule change was published for comment in the Federal Register on October 20, 2011.³ The Commission received seven comment letters on the proposed rule change – two from individual investors, three from an inter-dealer quotation system and two from a member firm.⁴ FINRA responded to comments on December 23, 2011.⁵

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 65568 (October 14, 2011), 76 FR 65307 (October 20, 2011) (Notice of Filing of File No. SR-FINRA-2011-058) (“Original Proposal”).

⁴ Letters to Elizabeth M. Murphy, Secretary, Commission, from Suzanne H. Shatto, Seattle, Washington, dated October 20, 2011; Naphtali M. Hamlet, Seattle, Washington, dated October 21, 2011; Daniel Zinn, General Counsel, OTC Markets Group, Inc., dated November 10, 2011; Michael T. Corrao, Managing Director, Knight Capital Group, Inc., dated November 16, 2011 (“Knight # 1”); R. Cromwell Coulson, President and CEO, OTC Markets, dated November 18, 2011; Daniel Zinn, General Counsel, OTC Markets Group, Inc., dated December 29, 2011; Michael T. Corrao, Managing Director, Knight Capital Group, Inc., dated January 13, 2012 (“Knight # 2”).

Comment letters are available at www.sec.gov.

⁵ On December 23, 2011, FINRA responded to comment letters received by the SEC as of that date. See letter to Elizabeth M. Murphy, Secretary, Commission, from Stephanie M.

The Commission published an order instituting proceedings pursuant to Section 19(b)(2)(B) of the Act,⁶ to determine whether to approve or disapprove the proposed rule change, in the Federal Register on January 24, 2012.⁷ The comment period closed on February 14, 2012, and FINRA's rebuttal period closed on February 28, 2012. The Commission received one comment letter in response to the Proceedings Order.⁸ On April 17, 2012, FINRA filed Amendment No. 1 to the proposed rule change. The text of Amendment No. 1 is available on FINRA's Web site at <http://www.finra.org>, at the principal office of FINRA and at the Commission's Public Reference Room.

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

As stated in the Original Proposal, FINRA is amending FINRA Rule 6433 (Minimum Quotation Size Requirements for OTC Equity Securities) (the "Rule") to, among other things, (1) simplify the tier structure, (2) parallel the approach taken by the national securities exchanges for securities priced at or above \$1.00, (3) expand the scope of the Rule to apply to all quotations or orders displayed on an inter-dealer quotation system, (4) incorporate the requirements of FINRA Rule 6434 (Minimum Pricing Increments for OTC Equity Securities)⁹ and, importantly, (5)

Dumont, Senior Vice President and Director of Capital Markets Policy, FINRA ("FINRA Response Letter").

⁶ 15 U.S.C. 78s(b)(2)(B).

⁷ See Securities Exchange Act Release No. 66168 (January 17, 2012), 77 FR 3515 (January 24, 2012) (Order Instituting Proceedings to Determine Whether to Disapprove File No. SR-FINRA-2011-058) ("Proceedings Order").

⁸ See letter to Elizabeth M. Murphy, Secretary, Commission, from Daniel Zinn, General Counsel, OTC Markets Group Inc., dated February 14, 2012.

⁹ See Securities Exchange Act Release No. 62359 (June 22, 2010), 75 FR 37488 (June 29, 2010) (File No. SR-FINRA-2009-054; "Order Approving NMS-Principled Rules for OTC Equity Securities"). FINRA Rule 6434 became effective on February 11, 2011 and FINRA Rule 6460 became effective on May 9, 2011. See Regulatory Notice 10-42 (September 2010).

facilitate the display of customer limit orders under FINRA Rule 6460 (Display of Customer Limit Orders) (the “limit order display rule”).¹⁰

In this Amendment No. 1, FINRA is modifying the Original Proposal in response to comment letters as well as further discussions with members, particularly with regard to the lower minimum dollar amount of displayed liquidity required under the proposed tiers.¹¹ For example, commenters expressed concern that the Original Proposal would remove meaningful minimum dollar value level requirements for displayed liquidity by market makers and suggested that any changes be implemented as a pilot.¹² FINRA believes that these proposed modifications, which increase several minimum tier sizes as compared to the Original Proposal, would address commenters’ concerns by increasing the minimum dollar commitment to the market overall, while nonetheless facilitating investor protection by providing for increased display of customer limit orders than is currently provided under the limit order display rule. As noted in the FINRA Response Letter, through the extension of limit order display for OTC equity securities, investors may now benefit from enhanced transparency of limit orders, improved prices and increased execution opportunities.¹³

¹⁰ See Order Approving NMS-Principled Rules for OTC Equity Securities.

¹¹ See, e.g., Knight # 1 and Knight # 2.

¹² See, e.g., Knight # 1 and Knight # 2.

¹³ As previously stated by the SEC, customer limit order display is beneficial to the markets:

The financial markets as a whole should benefit from [limit order display] because the price discovery process will be enhanced, market transparency will be improved and price competition will be promoted. By their very nature, these benefits are broad-based and pervasive.

Securities Exchange Act Release No. 36310 (September 29, 1995), 60 FR 52792 (October 10, 1995).

The minimum quotation sizes and liquidity ranges of the Original Proposal and the revised proposals are as follows:

Original Proposal

Tier Size Range		Min. Shares	Minimum Liquidity Range	
\$0.0001	0.0199	10,000	\$1.00	\$199.00
\$0.02	0.2599	1,000	\$20.00	\$259.90
\$0.26	0.5099	500	\$130.00	\$254.95
\$0.51	0.9999	200	\$102.00	\$199.98
\$1.00	174.99	100	\$100.00	\$17,499.00
\$175.00	---	1	\$175.00	---

Revised Proposal

Tier Size Range		Min. Shares	Minimum Liquidity Range	
\$0.0001	\$0.0999	10,000	\$1.00	\$999.00
\$0.10	\$0.1999	5,000	\$500.00	\$999.50
\$0.20	\$0.5099	2,500	\$500.00	\$1,274.75
\$0.51	\$0.9999	1,000	\$510.00	\$999.90
\$1.00	\$174.99	100	\$100.00	\$17,499.00
\$175.00	---	1	\$175.00	---

These revisions increase the minimum quotation sizes for price points between \$0.02 and \$1.00 (as compared to the Original Proposal). Specifically, the minimum quotation size required for securities priced between \$0.02 and \$0.0999 would be increased from 1,000 shares to 10,000 shares; between \$0.10 and \$0.1999 would be increased from 1,000 shares to 5,000 shares; between \$0.26 and \$0.5099 would be increased from 500 shares to 2,500 shares; and between \$0.51 and \$0.9999 from 200 shares to 1,000 shares. Therefore, under the revised tiers, for securities priced from \$0.10 up to \$1.00, the required minimum dollar value of displayed liquidity would range from \$500.00 to \$1,274.75 – dollar amounts FINRA believes represent

both appropriate minimum dollar value of displayed liquidity for members and reasonable dollar values for customer orders to be eligible for display on an inter-dealer quotation system.

Thus, FINRA believes that these revised tier sizes and corresponding liquidity minimum amounts are in the best interest of the market for OTC Equity Securities and investors in that they facilitate the display of additional liquidity by market makers and of approximately 95% of all customer limit orders reviewed.¹⁴ In addition, FINRA expects that – as the SEC has found in the context of its display rule – the improved display of customer limit orders resulting from the revised minimum quotation sizes will enhance the quality of published quotations for OTC Equity Securities and enhance competition and pricing efficiency in the market for OTC Equity Securities, which also should have a positive impact on capital formation.¹⁵

Further, FINRA believes that the resulting increased display of customer limit orders will improve the public availability of quotation information, increase quote competition, market efficiency, best execution and disintermediation.¹⁶

The revised tiers also would continue to yield the other benefits discussed in the Original Proposal, including simplifying the existing Rule by reducing the number of minimum quotation tiers from nine tiers to six tiers and requiring a round lot of one hundred shares for all securities priced at or above \$1.00.¹⁷

¹⁴ FINRA analyzed a random sample of over 100 million customer limit orders in OTC Equity Securities that were reported to FINRA during a six-month period.

¹⁵ See Securities Exchange Act Release No. 37619A, 61 FR 48290 (September 12, 1996) (“SEC Display Rule Adopting Release”).

¹⁶ See also SEC Display Rule Adopting Release.

¹⁷ A round lot of 100 shares applies to most NASDAQ and NYSE listed securities. The Commission notes that those OTC Equity Securities priced at or above \$175 are proposed to have a minimum quotation size that would equal the round lot size applicable to those securities, which is one share.

FINRA is proposing that the proposed rule change be implemented for all OTC Equity Securities displayed on an inter-dealer quotation system on a pilot basis for a period of one year from the effective date. The effective date of the minimum quotation size pilot will be 120 days from Commission approval. FINRA will provide the Commission with trading data, as necessary, to evaluate the impact of the pilot.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change, as amended by Amendment No. 1, is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-FINRA-2011-058 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-FINRA-2011-058. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those

that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2011-058 and should be submitted on or before [insert date 15 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹⁸

Kevin M. O'Neill
Deputy Secretary

¹⁸ 17 CFR 200.30-3(a)(57).