

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-66513; File No. SR-FINRA-2012-016)

March 5, 2012

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Allow FINRA to Exempt Certain Alternative Trading Systems from the Trade Reporting Obligation Under the Trade Reporting and Compliance Engine (“TRACE”) Reporting Rules

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 28, 2012, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as constituting a non-controversial rule change under Rule 19b-4(f)(6) under the Act,<sup>3</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

FINRA is proposing to adopt new Rule 6731 to provide FINRA with authority to exempt a member alternative trading system (“ATS”) that meets the specified criteria from the trade reporting obligation under the Rule 6700 Series. In addition, FINRA is proposing a conforming change to Rule 9610 to specify that FINRA has exemptive authority under proposed Rule 6731.

---

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 17 CFR 240.19b-4(f)(6).

The text of the proposed rule change is available on FINRA’s website 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 Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

A member that is a “Party to a Transaction” as defined in FINRA Rule 6710(e) in a transaction in a TRACE-Eligible Security must report the trade to TRACE under Rule 6730(a).<sup>4</sup> “Party to a Transaction” is defined as “an introducing broker-dealer, if any, an executing broker-dealer, or a customer.”<sup>5</sup> An ATS, which term includes electronic communications networks, is a Party to a Transaction and has a trade reporting obligation when a transaction in a TRACE-Eligible Security is executed through the ATS.<sup>6</sup>

---

<sup>4</sup> See Rule 6730(a). In transactions between members, each member must report the trade, and for transactions between a member and a customer, the member must report the trade.

<sup>5</sup> Under Rule 6710(e), “customer” includes a broker-dealer that is not a FINRA member.

<sup>6</sup> See [www.finra.org/Industry/Compliance/MarketTransparency/TRACE/FAQ/P125244#reporting](http://www.finra.org/Industry/Compliance/MarketTransparency/TRACE/FAQ/P125244#reporting) (FAQ: Who reports trades executed through electronic trading systems that are themselves broker-dealers? All FINRA members that are “parties to a transaction” have a trade reporting obligation under TRACE Rules. Where two FINRA members effect/execute a transaction through an electronic trading system that is

FINRA is proposing to adopt new Rule 6731 to provide FINRA with authority to exempt, upon application and subject to specified terms and conditions, a member ATS from the obligation to report a transaction in a TRACE-Eligible Security under certain limited circumstances. FINRA will only grant an exemption where all of the conditions set forth in the proposed rule are satisfied.

First, trades must be between ATS subscribers that are both FINRA members. For any trades between non-members, or a FINRA member and a customer (which includes a broker-dealer that is not a FINRA member), the exemption will not apply, and the ATS will have a trade reporting obligation under Rule 6730.

The ATS also must demonstrate that it meets the following criteria. First, the member subscribers must be fully disclosed to one another at all times on the ATS. Second, although the system brings together the orders of buyers and sellers and uses established, non-discretionary methods under which such orders interact with each other, the system does not permit automatic execution. A member subscriber must take affirmative steps beyond the submission of an order to agree to a trade with another member subscriber. Third, the trade does not pass through any ATS account, and the ATS does not in any way hold itself out to be a party to the specific trade. Fourth, the ATS does not exchange TRACE-Eligible Securities or funds on behalf of the member subscribers, take either side of the trade for clearing or settlement purposes, including, but not limited to, at DTC or otherwise, or in any other way insert itself into the trade.

In addition, the ATS and the member subscribers must acknowledge and agree in writing that the ATS shall not be deemed a party to the specific trade for purposes of trade reporting and that trades shall be reported by each member subscriber that satisfies the definition of “Party to a

---

registered as a broker-dealer, both members, as well as the electronic trading system would have a trade reporting obligation).

Transaction” under Rule 6710. An ATS that is granted an exemption must obtain such written agreements from all of its member subscribers prior to relying on the exemption.<sup>7</sup>

Finally, the ATS must agree to provide to FINRA on a monthly basis, or such other basis as prescribed by FINRA, data relating to the volume of trades in TRACE-Eligible Securities executed by the ATS’s member subscribers using the ATS’s system (e.g., number of trades, number of bonds (or notes, etc.) traded and total settlement value for each TRACE-Eligible Security traded). Importantly, although an ATS exempted under the proposed rule will not have trade reporting obligations under FINRA rules, the trading occurring through the ATS is still considered volume of the ATS for purposes of, among other things, the recordkeeping requirements of Rule 302 of SEC Regulation ATS<sup>8</sup> and determining whether the ATS triggers the Fair Access requirements under Rule 301(b)(5) of Regulation ATS or the Capacity, Integrity and Security of Automated Systems requirements of Rule 301(b)(6) of Regulation ATS, as applicable. The ATS also must acknowledge that failure to report such data to FINRA, in addition to constituting a violation of FINRA rules, will result in revocation of any exemption granted pursuant to the proposed rule change.

Where an exemption is granted, the ATS will not be deemed a Party to a Transaction for purposes of FINRA trade reporting rules and will not be identified in trade reports submitted to FINRA. As expressly stated in the proposed rule, the trade must be reported to FINRA by the

---

<sup>7</sup> FINRA reminds members of their books and records obligations under FINRA rules, the Exchange Act and applicable Exchange Act rules. Thus, any ATS that is granted an exemption under the proposed rule change would be required to retain the written agreements and be able to produce them to FINRA upon request.

<sup>8</sup> 17 CFR 242.300–303.

member subscribers that also are Parties to a Transaction under Rule 6710(e).<sup>9</sup> For example, FINRA member BD1 displays a quote through ATS X and member BD2 routes an order to BD1 for the price and size of BD1's quote using a messaging system provided by ATS X. BD1 does not subsequently re-route the order and executes the trade. Assuming that ATS X meets all of the criteria set forth in the proposed rule and has been granted an exemption by FINRA, it will not be deemed a Party to the Transaction for trade reporting purposes and should not be identified as such in the trade report submitted to FINRA. In this example, BD1 and BD2 would each have a reporting obligation under Rule 6730.

FINRA believes that the proposed rule change will reduce potential confusion and possible misreporting by clearly identifying the member with the trade reporting obligation in this instance. FINRA believes that an ATS that satisfies all conditions of the proposed rule change has a more limited involvement in the trade execution than the member subscribers and therefore the proposed exemption is appropriate in this narrow instance. FINRA expects that a large majority of ATSs will not qualify for the exemption, and the proposed rule change will not result in a change to their reporting.

FINRA also is proposing a conforming change to Rule 9610 to add proposed Rule 6731 to the list of rules pursuant to which FINRA has exemptive authority.

FINRA has filed the proposed rule change for immediate effectiveness and has requested that the SEC waive the requirement that the proposed rule change not become operative for 30 days after the date of the filing, such that FINRA can implement the proposed rule change on the date of filing.

---

<sup>9</sup> FINRA notes that where an ATS has been granted an exemption under the proposed rule, the member subscribers will be assessed the Trading Activity Fee under FINRA By-Laws, Schedule A, § 1. The ATS will not be assessed such fees.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>10</sup> which requires, among other things, that FINRA rules be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will reduce potential confusion and possible misreporting and enhance market transparency by clearly identifying the member with the trade reporting obligation under Rule 6730.

### B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest, (ii) impose any significant burden on competition, and, (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest, the proposed rule change has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>11</sup> and Rule 19b-4(f)(6) thereunder.<sup>12</sup>

---

<sup>10</sup> 15 U.S.C. 78o-3(b)(6).

<sup>11</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>12</sup> 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires FINRA to give the Commission written notice of its intent to file the proposed rule change, along with a

FINRA has asked the Commission to waive the 30-day operative delay so that the proposal may become operative immediately upon filing. The Commission believes that waiver of the operative delay is consistent with the protection of investors and the public interest. The proposed rule change is based on FINRA Rules 6183 and 6625, which provide FINRA authority to exempt certain ATSS from equity trade reporting. Those rules were recently proposed, noticed for public comment, and approved by the Commission.<sup>13</sup> The conditions and applicability of the proposed Rule 6731 are substantively identical. Therefore, the Commission designates the proposal operative upon filing.<sup>14</sup>

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

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or

---

brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Commission has waived the five-day prefiling requirement in this case.

<sup>13</sup> See Securities Exchange Act Release No. 65695 (November 4, 2011), 76 FR 70190 (November 10, 2011) (approving FINRA-2011-051).

<sup>14</sup> For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2012-016 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-2012-016. 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 website viewing and printing 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 publicly available. All submissions should refer to File Number SR-FINRA-2012-016 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>15</sup>

Kevin M. O'Neill  
Deputy Secretary

---

<sup>15</sup> 17 CFR 200.30-3(a)(12).