

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-76677; File No. SR-FINRA-2015-055)

December 17, 2015

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Provide FINRA with Authority to Grant Exemptions from TRACE Reporting Requirements for Certain ATS Transactions

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² notice is hereby given that on December 8, 2015, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“SEC” or “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 paragraph (f)(6) of Rule 19b-4 under the Act,³ which renders the proposal effective upon receipt of this filing by 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 the Substance of the Proposed Rule Change

FINRA is proposing to adopt new FINRA Rule 6732 to provide FINRA with authority to exempt certain transactions by a member alternative trading system (“ATS”) that meet specified criteria from the transaction reporting obligations under FINRA Rule 6730. In addition, FINRA is proposing a conforming change to FINRA Rule 9610 to specify that FINRA has exemptive authority under proposed Rule 6732.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 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

Rule 6730 (Transaction Reporting) generally requires that each FINRA member that is a party to a transaction in a TRACE-Eligible Security⁴ report the transaction to TRACE within the period of time prescribed in the rule. “Party to a transaction” means an introducing broker-dealer, if any, an executing broker-dealer or a customer.⁵ Thus, in transactions in a TRACE-Eligible Security between members, each member is a party to the transaction and is required to report the transaction. An ATS is a party to a transaction in a TRACE-Eligible Security

⁴ Rule 6710(a) provides that a “TRACE-Eligible Security” is a debt security that is United States dollar-denominated and issued by a U.S. or foreign private issuer, and, if a “restricted security” as defined in Securities Act Rule 144(a)(3), sold pursuant to Securities Act Rule 144A; or is a debt security that is U.S. dollar-denominated and issued or guaranteed by an Agency as defined in paragraph (k) or a Government-Sponsored Enterprise as defined in paragraph (n). “TRACE-Eligible Security” does not include a debt security that is: issued by a foreign sovereign, a U.S. Treasury Security as defined in paragraph (p), or a Money Market Instrument as defined in paragraph (o).

⁵ “Customer” includes a broker-dealer that is not a FINRA member.

occurring through its system and has a TRACE transaction reporting obligation, unless an exception or exemption applies.⁶

On February 28, 2012, FINRA adopted Rule 6731 (Exemption from Trade Reporting Obligation for Certain Alternative Trading Systems) to provide FINRA with authority to exempt ATSs from TRACE trade reporting obligations under certain circumstances; specifically, where the ATS demonstrates that: member subscribers are fully disclosed to one another at all times on the ATS; the system does not permit automatic execution (and a member subscriber must take affirmative steps beyond the submission of an order to agree to a trade with another member subscriber); 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 trade); and the ATS does not exchange TRACE-Eligible Securities or funds on behalf of the member subscribers or 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.⁷ In addition, trades on the ATS must be between subscribers that are both FINRA members. Where a Rule 6731 exemption is granted, the ATS is not deemed a party to the transactions occurring through its system for purposes of trade reporting requirements.⁸

⁶ See Regulatory Notice 14-53 (November 2014) (FINRA Reminds ATSs and ATS Subscribers of Their Trade Reporting Obligations in TRACE-Eligible Securities).

⁷ See Securities Exchange Act Release No. 66513 (March 5, 2012), 77 FR 14454 (March 9, 2012) (Notice of Filing and Immediate Effectiveness of File No. SR-FINRA-2012-016) (“Rule 6731 Proposal”).

⁸ FINRA stated in the Rule 6731 Proposal that an ATS that satisfies all the conditions of the proposal has a more limited involvement in the trade execution than the member subscribers and, therefore, the exemption from trade reporting is appropriate. As a condition to the proposed [sic] Rule 6731 exemption, the ATS and its member subscribers must acknowledge and agree in writing that the ATS is not deemed a party to the trade for purposes of trade reporting, and that trades shall be reported to FINRA in accordance with Rule 6730 by each member subscriber that satisfies the definition of “party to a transaction,” as defined in Rule 6710.

FINRA believes it is appropriate to propose a rule change to provide FINRA with authority to exempt trades on ATSs not otherwise falling within the exemption in Rule 6731 from the Rule 6730 trade reporting obligations. Pursuant to the proposed exemption, an ATS would not be required to report exempted transactions occurring on the ATS to TRACE, but rather, would be permitted to provide to FINRA on a monthly basis, or such other basis as prescribed by FINRA, data relating to each exempted trade occurring on the ATS. Each side of a trade for which an ATS is exempted from TRACE reporting pursuant to the proposal must be reported by a member (other than the ATS) that meets the definition of a “Party to a Transaction” identifying a contra-party (other than the ATS).

The proposal would permit FINRA to exempt a member ATS from reporting trades where: (a) the trade is between FINRA members, (b) the trade does not pass through any ATS account; (c) the ATS does not exchange TRACE-Eligible Securities or funds on behalf of the subscribers or 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; and (d) the ATS has entered into a written agreement with each member that is a “Party to a Transaction” with respect to any trade for which the ATS is exempted under this Rule, specifying that trades must be reported by such party pursuant to Rule 6730(c)(13) identifying the trade as having occurred on the ATS (using the ATS’s separate MPID obtained in compliance with Rule 6720(c)).⁹

Unlike the exemption provided for under Rule 6731 (where, if granted, all transactions occurring on the ATS are exempted from TRACE reporting), proposed Rule 6732 would provide

⁹ An ATS granted an exemption pursuant to the proposal would continue to be deemed a “party” to the transactions covered by the exemption, and would be required to remit to FINRA a transaction reporting fee. Specifically, member ATSs will be assessed a transaction reporting fee for each exempted transaction occurring through its system. Such fee will be assessed to the ATS once per exempt transaction, and will be calculated based upon the fee schedule set forth in Rule 7730(b)(1) for each exempt sell transaction.

FINRA authority to grant exemptions only for transactions that meet the enumerated criteria, which provides a greater degree of flexibility to member ATSs seeking an exemption. In addition, the proposed exemption omits two of the conditions required for relief under Rule 6731 — specifically, that member subscribers must be fully disclosed to one another at all times on the ATS, and that the system does not permit automatic execution and a member subscriber must take affirmative steps beyond the submission of an order to agree to a trade with another member subscriber. Thus, proposed Rule 6732 contemplates that an ATS may have a greater degree of involvement in exempted trades than contemplated by existing Rule 6731.¹⁰

In lieu of reporting through TRACE, proposed Rule 6732 would include a similar requirement to that contained in Rule 6731 in that it would require the periodic reporting of transaction information by any member ATS granted relief. Specifically, under the proposed exemption, an ATS would be required to provide FINRA with data relating to each exempted trade that occurred on its system (on a monthly basis or such other basis as prescribed by FINRA). FINRA will publish the required items of trade data information, the frequency of the reporting requirement, if different than monthly, and mode of transmission in a separate Regulatory Notice.¹¹

¹⁰ 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, Section 1. The ATS will not be assessed such fees with respect to any exempted trade.

¹¹ As is the case with Rule 6731, proposed Rule 6732 also provides that an ATS's failure to report required data to FINRA pursuant to Rule 6732, in addition to constituting a violation of FINRA rules, will result in revocation of any exemption granted pursuant to proposed Rule 6732. Similar to Rule 6731, volume in exempted trades occurring through the ATS would be considered volume of the ATS for purposes of, among other things, the recordkeeping requirements of Rule 302 of SEC Regulation ATS 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. See Rule 6731; see also 17 CFR 242.300-303.

FINRA believes that the proposed rule change will simplify compliance for member ATSs and other members. Specifically, where an ATS does not exchange TRACE-Eligible Securities or funds on behalf of the 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, and where the trade does not pass through any ATS account, the proposal provides FINRA with authority to allow ATSs (and member subscribers) to streamline their trade reporting practices.

In some cases, member subscribers trading on an ATS may prefer to program their back-end systems automatically to clear against the contra-party identified on TRACE trade reports. Thus, reporting against the contra-party member subscriber, rather than the ATS, would simplify clearance and settlement for such members. However, because, under FINRA rules, an ATS generally is deemed a party to each trade occurring through its system, Rule 6730 currently precludes member subscribers from reflecting a party other than the ATS on TRACE trade reports, even where the ATS has not inserted itself into the trade.

For example, today, where a member (BD 1) sells a TRACE-Eligible Security to another member (BD 2) through an ATS, Rule 6730 generally requires BD 1 to report a sale to the ATS and the ATS to report a buy from BD 1. The ATS also must report the corresponding sale to BD 2, and BD 2 must report its buy from the ATS.¹² Pursuant to the proposed exemption, where granted, an ATS would not be required to report the transactions with BD 1 and BD 2 to TRACE. In addition, BD 1 would be required to report to TRACE a sale to BD 2, identifying the trade as having occurred on the ATS, and BD 2 would be required to report to TRACE a buy from BD 1, identifying the trade as having occurred on the ATS on its TRACE report.

¹² In transactions between members, FINRA disseminates only the sale transaction.

Therefore, FINRA believes that the proposed rule change will simplify compliance for these member ATSS and their member subscribers without compromising public transparency in exempted trades, because the exempted transaction will continue to be trade reported by members and disseminated in accordance with existing rules.¹³ In addition, the requirement that any ATS granted an exemption pursuant to proposed Rule 6732 enter into a written agreement with each member that is a “Party to a Transaction” with respect to exempted trades, ensures that reporting members are aware that the ATS has been granted a Rule 6732 exemption and that exempted trades on the ATS are subject to different reporting requirements, specifically, that the reporting member identify a party other than the ATS as its contra-party and identify the ATS on which the trade had occurred in its TRACE reports.

FINRA has filed the proposed rule change for immediate effectiveness. The implementation date of the proposed rule change will be July 18, 2016.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹⁴ which requires, among other things, that FINRA rules must 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 simplify compliance for certain ATSS and their member subscribers by permitting subscribers to trade report with the party against which it will clear the trade. The proposal also accommodates a broader range of ATS models. FINRA also notes that public transparency with respect to exempted trades will not be

¹³ FINRA also is proposing a conforming change to Rule 9610 to add proposed Rule 6732 to the list of rules pursuant to which FINRA has exemptive authority.

¹⁴ 15 U.S.C. 78o-3(b)(6).

compromised because such transactions will continue to be trade reported by members and disseminated in accordance with existing rules.

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. Any ATS that meets the criteria set forth in the proposed rule may apply for the exemption with respect to eligible transactions occurring on its platform. In addition, irrespective of an ATS's model or whether the ATS is granted an exemption pursuant to this proposal, all ATSs that are a "party to a transaction" must continue to pay transaction reporting fees with respect to Rule 6732 exempted transactions. As stated above, any ATS granted a Rule 6732 exemption would continue to be deemed a "party" to the transactions covered by the exemption, and would be required to remit to FINRA a transaction reporting fee based on the fee schedule set forth in Rule 7730(b)(1) for each exempted sell transaction occurring through the ATS.

Economic Impact Assessment

Need for the Rule

As discussed above, an ATS is a party to a transaction in TRACE-eligible securities occurring on that ATS. As such, an ATS is responsible to report the transaction to FINRA as provided in Rule 6730, unless an exception or exemption applies.

FINRA recognizes that there are different business models for the way an ATS may facilitate trading on its platform, and the functional role of the ATS may differ in each of these models. For instance FINRA is aware that some ATS's do not pass TRACE-eligible securities or funds through their own accounts as part of an execution. In instances where the functional activities of the ATS are more limited with respect to a transaction, FINRA believes that the

ATS, while still party to the transaction, may benefit from a streamlined reporting regime without reducing public transparency.

Economic Baseline

By FINRA rule today, all ATSs are parties to transactions in TRACE-eligible securities occurring on the ATS and are subject to TRACE reporting. Rule 6731 provides FINRA authority to exempt an ATS from Rule 6730 TRACE transaction reporting requirements where an ATS meets the conditions in Rule 6731 described above. Thus, an ATS that does not meet the conditions of Rule 6731 is required to report transactions occurring on the ATS to TRACE in accordance with FINRA rules.

Economic Impacts

FINRA estimates that only a small number of ATSs would be eligible to seek the exemption based on staff understanding of their current business models, although the proposed exemption would be available to any current or future ATS that would meet the requirements. Member subscribers who execute trades on an ATS that seeks and is granted the proposed exemption also may be impacted. FINRA does not have a reliable estimate for the number of transactions that might be eligible for the exemption.

Benefits of the Rule

Any ATS that meets the qualifications proposed in this rule may request exemption from FINRA. Where granted, the ATS would presumably reduce its compliance costs by shifting from contemporaneous reporting of transactions to TRACE in TRACE-eligible securities to periodic reporting.

Costs of the Rule

An ATS that seeks and is granted an exemption under this proposed rule may incur costs to modify its systems, and must update its policies and procedures to reflect reporting consistent with the periodic regime. Each ATS may determine independently whether or not it seeks to obtain the exemption, and thus, it is likely that an ATS would only seek this exemption where it was less costly than meeting its current reporting requirements.

FINRA understands that a commenter to a related filing indicated that transactions in TRACE-eligible securities occurring on some ATSs are “given up” to the broker-dealer counterparties for TRACE reporting.¹⁵ Notwithstanding this comment, the reporting obligations to the ATS remain, so any costs to an ATS associated with this proposal should be measured from the baseline of that obligation.

Where an ATS seeks and is granted the exemption, member subscribers who transact through the ATS also may incur costs associated with reporting the additional information to FINRA that identifies the ATS where the trade occurred. These costs may include additional programming and testing along with updating policies and procedures. FINRA notes, however, that member subscribers may determine where to seek executions and would not have to incur the related costs if they choose to send orders elsewhere for execution.

Both member subscribers and ATSs may incur additional costs associated with creating and maintaining a written agreement with respect to the reporting of any trades for which the ATS is exempted under the proposed rule.

¹⁵ See Securities Exchange Act Release No. 71341 (January 17, 2014), 79 FR 4213 at 4217 (January 24, 2014) (Order Approving File No. SR-FINRA-2013-042).

Related Economic Impacts

FINRA also considered the potential impacts of the proposed rule on investors and other parties that might rely on TRACE reporting. As proposed, the rule would not negatively impact FINRA's ability to monitor securities markets. The proposed rule would not substantively reduce the information collected by FINRA on TRACE-eligible securities transactions occurring on an ATS. Member subscribers maintain their obligation to report transactions on the ATS to TRACE within the time prescribed by FINRA rules. The additional information collected pursuant to the exemption under the rule would enhance FINRA's ability to identify all exempted trades occurring on an individual ATS. Further, the exemption would not impact the quality and completeness of the information made generally available through TRACE, since TRACE reporting obligations continue to apply to the member subscribers transacting on the ATS.

Alternatives Considered

The primary alternative considered was to continue to have ATS [sic] with business models meeting the proposed exemptive criteria continue to report as they do today. However, FINRA concluded that the proposed exemption is a reasonable approach that may simplify compliance for some members without degrading the quality and completeness of information available to FINRA and the public.

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, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁶ and Rule 19b-4(f)(6) thereunder.¹⁷

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. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

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
- Send an e-mail to rule-comments@sec.gov. Please include File No. SR-FINRA-2015-055 on the subject line.

¹⁶ 15 U.S.C. 78s(b)(3)(A).

¹⁷ 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6) requires a self-regulatory organization to give the Commission written notice of its intent to file the proposed rule change, along with a 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. FINRA has satisfied this requirement.

Paper comments:

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

All submissions should refer to File No. SR-FINRA-2015-055. 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, D.C. 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 No. SR-FINRA-2015-055, 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.¹⁸

Robert W. Errett
Deputy Secretary

¹⁸ 17 CFR 200.30-3(a)(12).