

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-59905; File No. SR-FINRA-2007-012)

May 12, 2009

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change, as Modified by Amendment Nos. 1 and 2 Thereto to Amend Trade Reporting Rules to Require a Related Market Center Indicator on Certain Non-Tape Reports Submitted to FINRA

I. Introduction

On September 12, 2007, the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“Commission”), 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> a proposed rule change to amend its trade reporting rules to require members to record a related market center indicator on certain non-tape reports submitted to FINRA. On December 18, 2007, FINRA filed Amendment No. 1 to the proposed rule change. The proposed rule change, as modified by Amendment No. 1, was published for comment in the Federal Register on December 28, 2007.<sup>3</sup> The Commission received three comments on the proposal.<sup>4</sup> FINRA filed Amendment No. 2 on March 27, 2009.<sup>5</sup> This order approves to the proposed rule change, as

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

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

<sup>3</sup> See Securities Exchange Act Release No. 57020 (December 20, 2007), 72 FR 73930 (“Notice”).

<sup>4</sup> See letter from Securities Industry and Financial Markets Association, dated January 24, 2008 (“SIFMA Letter”); letter from Citigroup Global Markets, Inc., dated February 1, 2008 (“Citi Letter”); and letter from Financial Information Forum, dated February 29, 2008 (“FIF Letter”).

<sup>5</sup> In Amendment No. 2, FINRA: (1) addressed the comments received in response to the publication of the Notice and proposed certain minor modifications and clarifications in response to the comments; (2) reflected changes to the underlying rule text adopted pursuant to two intervening rule changes and made conforming modifications to the

modified by Amendment Nos. 1 and 2.

## II. Description of the Proposal

As discussed more fully in the Notice, certain transactions can be reported in related tape (i.e., the transaction is reported to the tape for publication) and non-tape reports.<sup>6</sup>

Thus, agency transactions where one member acts as agent on behalf of another member can be reported in related tape and non-tape reports. Similarly, a riskless principal transaction,<sup>7</sup> which is a functional equivalent of an agency trade, can be submitted to FINRA as a single trade report properly marked as riskless principal, or as two separate reports: (1) a tape report to reflect the initial leg of the transaction and (2) a non-tape report to reflect the offsetting, “riskless” leg of the transaction. Currently, a non-tape report does not provide specific information pertaining to the related tape report.

FINRA proposed to amend FINRA Rules 7130 (relating to the ADF/TRACS), 7230A (relating to the FINRA/NASDAQ TRF), 7230B (relating to the FINRA/NYSE TRF), and 7330 (relating to OTC RF)<sup>8</sup> to require members for any non-tape report (either a non-tape, non-clearing report or a clearing-only report) submitted to a FINRA Facility associated with a

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proposed rule change. This Amendment is a technical amendment and therefore not subject to notice and comment.

<sup>6</sup> Non-tape reports can be (1) “non-tape, non-clearing,” i.e. the transaction is not reported to the tape but is submitted to FINRA for regulatory (not clearing) purposes, or (2) “clearing-only,” i.e., the transaction is not reported to the tape and is submitted to FINRA for clearing (and perhaps also regulatory) purposes.

<sup>7</sup> For purposes of over-the-counter trade reporting requirements applicable to equity securities, a “riskless principal” transaction is a transaction in which a member, after having received an order to buy (sell) a security, purchases (sells) the security as principal (the initial leg) and satisfies the original order by selling (buying) as principal at the same price (the offsetting, “riskless” leg). See FINRA Regulatory Notice 07-38 (August 2007).

<sup>8</sup> The original filing contained different Rule numbers, which were revised in Amendment No. 2 to account for intervening rule filings. See supra note 5.

previously executed trade that was not reported to that same FINRA Facility, to identify the facility or market to which the associated trade was reported. The proposed rule change also requires that members retain and produce to FINRA, upon request, documentation relating to the associated trade (e.g., a confirmation from the exchange identifying the “street side” of a riskless principal transaction).

FINRA also proposed that where a single non-tape report is related to multiple tape reports: (1) if the multiple tape reports were made to a single exchange or, in the case of over-the-counter trades, a single FINRA Facility, that exchange or facility must be properly reflected on the single non-tape report; and (2) if the multiple tape reports were made to different exchanges and/or FINRA Facilities, the member will not be required to identify the specific exchanges or facilities; it will be required to populate the Related Market Center field with a standard indicator: “multiple venues.”<sup>9</sup> In addition, where a member routes an order and has no basis for identifying where the trade was ultimately executed or, in the case of over-the-counter trades, where the trade was ultimately reported, the member will be required to populate the Related Market Center field with a standard indicator: “unknown venue.”<sup>10</sup>

### III. Discussion

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities association.<sup>11</sup> In particular, the Commission finds that the proposed rule change is

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<sup>9</sup> See Amendment No. 2.

<sup>10</sup> See id.

<sup>11</sup> In approving these proposed rule changes, the Commission has considered the proposed rules' impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

consistent with Section 15A(b)(6) of the Act,<sup>12</sup> in that it is designed, among other things, to prevent fraudulent and manipulative acts and practices; to promote just and equitable principles of trade; to remove impediments to and perfect the mechanism of a free and open market and a national market system; and, in general, to protect investors and the public interest.

The Commission believes that the proposed rule change will result in a more complete and accurate audit trail and ensure that members are not using non-tape reports to circumvent FINRA or Commission rules. FINRA stated that currently it is difficult to determine with certainty where the associated trade was reported, especially if that trade was reported to an exchange or another FINRA Facility.<sup>13</sup>

As noted above, the Commission received three comment letters in response to the Notice.<sup>14</sup> The three commenters generally oppose the proposal and state that the potential costs, including required system changes, outweigh the benefits of the proposal. In addition, the commenters raise several concerns about the practical difficulties of complying with the proposed rule change. First, the commenters indicate it would be difficult (if not impossible) to identify multiple exchanges and/or FINRA Facilities where a single non-tape report is associated with multiple executions on multiple markets. Second, the three commenters point out that when a firm routes an order, it may not know the ultimate execution destination. Third, the commenters argue that even if a firm knows that a trade in an NMS stock was executed over-the-

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<sup>12</sup> 15 U.S.C. 78o-3(b)(6).

<sup>13</sup> Currently, FINRA must manually match non-tape reports with associated tape reports for purposes of monitoring member compliance with trade reporting rules. FINRA stated that by requiring that firms identify the market center or facility to which the associated tape report was submitted, the universe of tape reports that must be reviewed as part of the matching process will be significantly narrowed, and accordingly, the effectiveness and certainty of the matching process will be enhanced.

<sup>14</sup> See supra note 4.

counter, the firm may not know where the trade was reported because FINRA's Uniform Service Bureau/Executing Broker Agreement ("USBEB") allows the reporting party to report to any TRF or ADF, without providing notice to the other party to the trade.<sup>15</sup>

FINRA replied to the comments in Amendment No. 2 and revised and clarified the original proposal to alleviate the commenters' concerns. In particular, FINRA clarified that where a single non-tape report is related to multiple tape reports: (1) if the multiple tape reports were made to a single exchange or, in the case of over-the-counter trades, a single FINRA Facility, that exchange or facility must be reflected on the single non-tape report; and (2) if the multiple tape reports were made to different exchanges and/or FINRA Facilities, the member will be required to populate the Related Market Center field with a standard indicator: "multiple venues."<sup>16</sup> In addition, FINRA provided that where a member routes an order and has no basis for identifying the relevant exchange or FINRA Facility to determine where the trade was ultimately executed or, in the case of over-the-counter trades, where the trade was ultimately reported, the member will be required to populate the Related Market Center field with a standard indicator: "unknown venue."

To the extent technological enhancements are required, FINRA stated that it intends to provide adequate time for members to make the necessary changes and revised the original proposal to provide for the implementation of the proposed rule change at least 90 days following implementation on August 3, 2009, of the amendments to FINRA trade reporting rules adopted pursuant to SR-FINRA-2008-011.<sup>17</sup>

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<sup>15</sup> See SIFMA Letter and Citigroup Letter.

<sup>16</sup> See Amendment No. 2.

<sup>17</sup> See FINRA Regulatory Notice 09-08 (January 2009).

The Commission believes that FINRA's approach that tailors the proposed reporting requirement to reflect informational limitations described by the commenters is reasonable, in that it reflects FINRA's expectation that members provide as much information as is reasonably available at the time the non-tape report is submitted. Further, the Commission notes that FINRA clarified that where a member routes to an exchange and has a reasonable basis for reporting that the trade was executed on that exchange, FINRA would not consider it a violation if, unbeknownst to the member, the trade is ultimately executed somewhere other than the routed exchange.<sup>18</sup> The Commission also notes that it would expect FINRA to incorporate the proposed changes into its surveillance and examination programs to ensure that members are not improperly using the "multiple venue" or "unknown venue" indications.

#### IV. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with the Act and the rules and regulations thereunder applicable to a national securities association.

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<sup>18</sup> The same approach would apply to reporting to other FINRA Facilities.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>19</sup> that the proposed rule change (SR-FINRA-2007-012), as modified by Amendment Nos. 1 and 2 thereto, be and hereby is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>20</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>19</sup> 15 U.S.C. 78s(b)(2).

<sup>20</sup> 17 CFR 200.30-3(a)(12).