

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-87725; File No. SR-FINRA-2019-029)

December 12, 2019

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Modify the Securities Transaction Credits Applicable to FINRA/Nasdaq TRF Participants

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 5, 2019, 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, II, and III below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as “establishing or changing a due, fee or other charge” under Section 19(b)(3)(A)(ii) of the Act³ and Rule 19b-4(f)(2) thereunder,⁴ 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 Substance of the Proposed Rule Change

FINRA is proposing to amend FINRA Rule 7610A to modify the securities transaction credits that apply to FINRA members that utilize the FINRA/Nasdaq Trade Reporting Facility Carteret (the “FINRA/Nasdaq TRF Carteret”) and the FINRA/Nasdaq Trade Reporting Facility Chicago (the “FINRA/Nasdaq TRF Chicago”) (collectively, the “FINRA/Nasdaq TRFs”).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A)(ii).

⁴ 17 CFR 240.19b-4(f)(2).

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

The FINRA/Nasdaq TRFs are facilities of FINRA that are operated by Nasdaq, Inc. ("Nasdaq"). In connection with the establishment of the FINRA/Nasdaq TRFs, FINRA and Nasdaq entered into a limited liability company agreement (the "LLC Agreement"). Under the LLC Agreement, FINRA, the "SRO Member," has sole regulatory responsibility for the FINRA/Nasdaq TRFs. Nasdaq, the "Business Member," is primarily responsible for the management of the FINRA/Nasdaq TRFs' business affairs, including establishing pricing for use of the FINRA/Nasdaq TRFs, to the extent those affairs are not inconsistent with the regulatory and oversight functions of FINRA. Additionally, the Business Member is obligated to pay the cost of regulation and is entitled to the profits and losses, if any, derived from the operation of the FINRA/Nasdaq TRFs.

Pursuant to FINRA Rule 7610A, FINRA members that report over-the-counter (“OTC”) trades in NMS stocks to the FINRA/Nasdaq TRFs (“Participants”) may qualify for revenue sharing payments, in the form of transaction credits, based upon those transactions that are attributable to such Participants.⁵ This rule is administered by Nasdaq, in its capacity as the Business Member and operator of the FINRA/Nasdaq TRFs on behalf of FINRA.⁶

Rule 7610A sets forth tiered schedules of transaction credits that describe, for reports in transactions in each Tape (A, B and C), the percentage of attributable revenue sharing that a Participant will receive if it achieves specified percentages of market share. The schedules provide for “Retail Participants”⁷ to receive higher revenue sharing percentages than other FINRA members at the two lowest tiers for transactions in each Tape. For reference purposes, the existing transaction credit schedules are as follows:

Tape A

<u>Percentage Market Share</u>	<u>Percent of attributable revenue shared</u>	<u>Percent of attributable revenue shared (Retail Participants)</u>
Greater than or equal to 2%	98%	98%
Less than 2% but greater than or equal to 1%	95%	95%
Less than 1% but greater than or equal to 0.50%	75%	75%

⁵ A transaction is attributable to a Participant if the Participant is identified as the Executing Party in a trade report submitted to a FINRA/Nasdaq TRF that the FINRA/Nasdaq TRF subsequently submits to the Consolidated Tape Association or the Nasdaq Securities Information Processor. Credits are paid on a quarterly basis.

⁶ FINRA’s oversight of this function performed by the Business Member is conducted through a recurring assessment and review of TRF operations by an outside independent audit firm.

⁷ Supplementary Material .01 to Rule 7620A defines a “Retail Participant” as a “participant in the FINRA/Nasdaq Trade Reporting Facility for which substantially all of its trade reporting activity on the FINRA/Nasdaq Trade Reporting Facility comprises Retail Orders.” The term “Retail Order” is also defined under Rule 7620A.01.

Less than 0.50% but greater than or equal to 0.10%	20%	75%
Less than 0.10%	0%	75%

Tape B

<u>Percentage Market Share</u>	<u>Percent of attributable revenue shared</u>	<u>Percent of attributable revenue shared (Retail Participants)</u>
Greater than or equal to 2%	98%	98%
Less than 2% but greater than or equal to 1%	90%	90%
Less than 1% but greater than or equal to 0.35%	70%	70%
Less than 0.35% but greater than or equal to 0.10%	10%	70%
Less than 0.10%	0%	70%

Tape C

<u>Percentage Market Share</u>	<u>Percent of attributable revenue shared</u>	<u>Percent of attributable revenue shared (Retail Participants)</u>
Greater than or equal to 2%	98%	98%
Less than 2% but greater than or equal to 1%	95%	95%
Less than 1% but greater than or equal to 0.50%	75%	75%
Less than 0.50% but greater than or equal to 0.10%	20%	75%
Less than 0.10%	0%	75%

Nasdaq, as the Business Member, has determined to modify the schedule of transaction credits applicable to the FINRA/Nasdaq TRFs to provide a more competitive distribution of pricing incentives and benefits among Participants to the extent that they engage in a substantial volume of Executing Party activity. The proposed amended schedule is also designed to be more

competitive with the schedule of transaction credits applicable to the other FINRA TRF.⁸

FINRA proposes to amend Rule 7610A accordingly.

The proposed rule change would amend the third revenue sharing tier for both Retail and non-Retail Participants (i.e., Participants that achieve market shares of less than 1.0% but greater than or equal to 0.50% for Tape A and C securities, and less than 1.0% but greater than or equal to 0.35% for Tape B securities) by increasing the percentage of revenue shared with Participants that qualify for the tier. Specifically, Participants that achieve a market share of less than 1.0% but greater than or equal to 0.50% in securities in Tapes A and C (or greater than or equal to 0.35% for Tape B securities) will be eligible to receive 85% of attributable revenues for securities in all Tapes.

Nasdaq, as the Business Member, estimates that 13 Participants currently qualify for the existing revenue sharing tier. Assuming that these Participants continue to qualify for this tier, Nasdaq estimates, based on current trade reporting activity, that all of these Participants will experience an increase in the amount of the credits that they receive. Based on a review of trade reporting activity for the period July 2018 to June 2019, Nasdaq estimates that these Participants could potentially receive between \$10,000 and \$190,000 more credits than they receive today. No new product or service will accompany the proposed changes to revenue sharing credits.

FINRA has filed the proposed rule change for immediate effectiveness. The operative date will be January 1, 2020.

⁸ Pursuant to FINRA Rule 7610B, the FINRA/NYSE TRF presently shares with its participants, for all Tapes, 100% of attributable revenue for market shares greater than or equal to 2.0%, 95% of attributable revenue for market shares greater than or equal to 0.5% but less than 2.0%, 85% of attributable revenue for market shares greater than or equal to 0.1% but less than 0.5%, and 0% of attributable revenue for market shares of less than 0.1%.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(5) of the Act,⁹ which requires, among other things, that FINRA rules provide for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system that FINRA operates or controls. All similarly situated members are subject to the same fee structure and access to the FINRA/Nasdaq TRFs is offered on fair and nondiscriminatory terms.

The Proposal is Reasonable

The proposed change to modify the revenue sharing credits for the FINRA/Nasdaq TRFs is reasonable in several respects. As a threshold matter, the FINRA/Nasdaq TRFs are subject to significant competitive forces in the market for trade reporting services for OTC trades in NMS stocks that constrain its pricing determinations in that market. The competing FINRA TRF presently offers a similar tiered pricing structure to that of the FINRA/Nasdaq TRFs, including a schedule of revenue sharing credits that apply based upon its participants achieving certain levels of market share.¹⁰ Participants can freely and do shift their trade reporting activity between the various FINRA TRFs in response to pricing, product or service changes. The proposed rule change renders more generous the FINRA/Nasdaq TRFs' revenue sharing credits to maintain and increase activity and market share.

⁹ 15 U.S.C. 78o-3(b)(5).

¹⁰ Because the FINRA/Nasdaq TRFs and the FINRA/NYSE TRF are operated by different business members competing for market share, FINRA does not take a position on whether the pricing for one TRF is more favorable or competitive than the pricing for the other TRF.

The Proposal is an Equitable Allocation of Credits and Charges

The proposed rule change will allocate revenue sharing credits fairly among FINRA/Nasdaq TRF Participants. Nasdaq, as the Business Member, has determined to increase the revenue sharing credits that the FINRA/Nasdaq TRFs offer to their Participants as a means of rewarding those Participants that engage in substantial amounts of trade reporting activity on the FINRA/Nasdaq TRFs, reducing the costs to such Participants of reporting trades to the FINRA/Nasdaq TRFs, and improving the competitive standing of the FINRA/Nasdaq TRFs relative to their competitor, which offers similar credits to its participants. Nasdaq believes it is equitable to target such increases only to Participants with market shares of less than 1.0% but greater than or equal to 0.50% (for securities in Tapes A and C) and 0.35% (for securities in Tape B). The tier selected accounts for 5% of the Transaction Credit eligible Participant base and 17% of trade reporting volume of the FINRA/Nasdaq TRFs and it is a tier that is particularly vulnerable to competition from the other FINRA TRF, which presently offers to share 95% of attributable revenues with its participants that achieve market shares of equal to or greater than 0.5% and less than 2.0%. The proposed rule change will render the FINRA/Nasdaq TRFs more competitive with its competitors in terms of revenue sharing for Participants in this market segment.

The Proposal is not Unfairly Discriminatory

The proposed rule change is not unfairly discriminatory. As an initial matter, nothing about the volume-based tiered pricing model of the FINRA/Nasdaq TRFs is inherently unfair. Instead, it is a rational pricing model that is well-established and ubiquitous in today's economy among firms in various industries – from co-branded credit cards to grocery stores to cellular telephone data plans – that use it to reward the loyalty of their best customers that provide high

levels of business activity and incent other customers to increase the extent of their business activity. It is also a pricing model that FINRA TRFs have long employed under FINRA rules filed with the Commission.

Nasdaq, as the Business Member, intends for the proposal to increase incentives to FINRA/Nasdaq TRF Participants to engage in substantial trade reporting activity on the FINRA/Nasdaq TRFs. The increased incentive will be available to all Participants with market shares of less than 1.0% but greater than or equal to 0.50% (Tapes A and C securities) and 0.35% (Tape B securities).

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

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

Intramarket Competition

Nasdaq, as the Business Member, does not believe that the proposed rule change will place any category of Participant at a competitive disadvantage. As discussed above, all Participants that currently qualify for credits will continue to qualify for credits under the proposed rule change and will receive higher rates of credits than they do today. Meanwhile, Participants that do not qualify for the proposed tiers (or that do not qualify for the higher of the proposed tiers) may grow or modify their businesses so that they will do so. Participants are free to report their OTC trades in NMS stocks to the competing TRF to the extent they believe that the credits provided are not attractive. Price competition between the TRFs is substantial, with trade reporting activity and market share moving freely between them in reaction to fee and credit changes.

Intermarket Competition

Nasdaq believes that the proposed modifications to the schedule of credits applicable to the FINRA/Nasdaq TRFs will not impose a burden on competition among the FINRA trade reporting facilities because use of the FINRA/Nasdaq TRFs is completely voluntary and subject to competition.¹¹ Currently, with the exception of FINRA/Nasdaq TRF Retail Participants in the lowest tier, the competing FINRA TRF provides higher transaction credits to its participants than the FINRA/Nasdaq TRFs for engaging in similar levels of trade reporting activity. Nasdaq, as the Business Member, seeks to increase the credits that the FINRA/Nasdaq TRFs provide to market participants so that these credits are more competitive. Nasdaq believes that the proposed increase in credits is necessary to retain reported volume. Indeed, firms that report OTC trades in NMS stocks can readily favor competing facilities if they deem fee levels at a particular facility to be excessive, or credit opportunities available at other facilities to be more favorable.

The competition, in turn, is free to modify its own fees and credits in response to this proposed rule change to maintain or increase its attractiveness to participants. Accordingly, Nasdaq believes that the risk that this proposed rule change will impose any burden on intermarket competition is extremely limited.

If market participants determine that the changes proposed herein are inadequate or unattractive, it is likely that the FINRA/Nasdaq TRFs will lose market share as a result. Accordingly, the proposed rule change will not impair the ability of the other FINRA TRF to maintain its competitive standing.

¹¹ Because the FINRA/Nasdaq TRFs and the FINRA/NYSE TRF are operated by different business members competing for market share, FINRA does not take a position on whether the pricing for one TRF is more favorable or competitive than the pricing for the other TRF.

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

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A) of the Act¹² and paragraph (f)(2) of Rule 19b-4 thereunder.¹³ 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 Number SR-FINRA-2019-029 on the subject line.

¹² 15 U.S.C. 78s(b)(3)(A).

¹³ 17 CFR 240.19b-4(f)(2).

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 Number SR-FINRA-2019-029. 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. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make

available publicly. All submissions should refer to File Number SR-FINRA-2019-029 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.¹⁴

J. Matthew DeLesDernier
Assistant Secretary

¹⁴ 17 CFR 200.30-3(a)(12).