

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-76061; File No. SR-FINRA-2015-035)

September 30, 2015

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change Relating to the Submission of “Clearing-Only, Non-Regulatory Reports” to the FINRA Equity Trade Reporting Facilities

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 September 22, 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, II, and III 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 amend FINRA rules governing the reporting of over-the-counter (“OTC”) transactions in equity securities to the FINRA Facilities⁴ to allow the submission of

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 17 CFR 240.19b-4(f)(6).

⁴ For purposes of this filing, the FINRA Facilities are the Alternative Display Facility (“ADF”) and the Trade Reporting Facilities (“TRF”), to which members report OTC transactions in NMS stocks, as defined in SEC Rule 600(b) of Regulation NMS; and the OTC Reporting Facility (“ORF”), to which members report transactions in “OTC Equity Securities,” as defined in Rule 6420 (i.e., non-NMS stocks such as OTC Bulletin Board and OTC Market securities), as well as transactions in Restricted Equity Securities, as

“clearing-only, non-regulatory reports,” as defined herein, relating to previously executed and reported transactions and exempt such reports from certain reporting requirements under FINRA rules.

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

Background

With limited exceptions, FINRA trade reporting rules require that members report OTC transactions in equity securities by submitting a “tape” report (the transaction is reported for public dissemination purposes) to FINRA.⁵ In some instances, members may be required (or

defined in Rule 6420, effected pursuant to Securities Act Rule 144A.

⁵ FINRA trade reporting rules require that for transactions between members, the “executing party” report the trade to FINRA. For transactions between a member and a non-member or customer, the member must report the trade. “Executing party” is defined under FINRA rules as the member that receives an order for handling or execution or is presented an order against its quote, does not subsequently re-route the

may choose) to also submit one or more “non-tape” reports (the transaction is not reported for publication) in connection with the transaction. For example, members executing OTC transactions as riskless principal⁶ or agent on behalf of other members are required to submit non-tape report(s) to identify other FINRA members that are parties to the trade.⁷ Non-tape reports can be (1) “non-tape, non-clearing” (the transaction is not reported to the tape and is submitted to FINRA solely for regulatory purposes) or (2) “clearing-only” (the transaction is not reported to the tape and is submitted to FINRA for clearing (and perhaps also regulatory purposes)). FINRA notes that members can elect, but are not required, to have the FINRA Facility submit their trades to the National Securities Clearing Corporation (“NSCC”) for clearance and settlement, and in such instance, they would designate the submission for clearing.⁸

Effective February 2, 2015, any member operating an alternative trading system (“ATS”) must obtain for each such ATS a single, unique market participant identifier (“MPID”) that is designated for exclusive use for reporting the ATS’s transactions.⁹ The member must use such separate MPID to report all transactions executed within the ATS to FINRA. Members that

order, and executes the transaction. See Rules 6282(b), 6380A(b), 6380B(b) and 6622(b).

⁶ For purposes of OTC 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.

⁷ See Rules 6282(d)(4), 6380A(d)(4), 6380B(d)(4) and 6622(d)(4).

⁸ As noted, FINRA rules do not mandate that members submit OTC transactions for clearing through a FINRA Facility, and for example, members may elect to clear via direct submission to the NSCC by a Qualified Special Representative (“QSR”).

⁹ See Rules 6160, 6170 and 6480.

operate multiple ATSS or engage in other lines of business requiring the use of MPIDs must obtain and use multiple MPIDs.

Following implementation of the ATS MPID requirement, some firms that operate an ATS and use a FINRA Facility to submit trades to NSCC submit separate clearing-only reports to FINRA using their main broker-dealer MPID. In other words, the firm submits a tape report and any required non-tape, non-clearing (i.e., regulatory) reports using the ATS MPID, and also submits one or more separate clearing-only reports using the firm's main broker-dealer MPID. FINRA understands that firms report in this manner to facilitate externally facing back office clearing processes, such as client reporting and step-out trade processing, that are built using the firm's main broker-dealer MPID. Firms have indicated that it would be a significant burden to change these established clearing processes and use the ATS MPID for purposes of clearing-only submissions.

Currently, these additional clearing reports with the firm's main broker-dealer MPID duplicate the trade information previously reported to FINRA. Because they are not identified with the same MPID and are not linked to the related tape and non-tape, non-clearing reports, FINRA is unable to distinguish duplicative clearing-only reports from other reports that are submitted to satisfy a firm's regulatory reporting obligations. This creates confusion in the audit trail which in turn can result in the generation of false alerts in FINRA's automated surveillance programs.

Clearing-Only, Non-Regulatory Reports

After reviewing the system capabilities and consulting with industry representatives, FINRA is proposing to adopt new subparagraph (4) under Rules 7130(g), 7230A(i), 7230B(h) and 7330(h) to create a uniquely identified category of submissions to FINRA that are "clearing-

only, non-regulatory reports,” i.e., the transaction is submitted solely to facilitate clearing and not for dissemination or regulatory purposes. As described in more detail below, ATs would be permitted to use their main broker-dealer MPID on this limited subset of reports.

Pursuant to the proposed rule change, a member may submit a clearing-only, non-regulatory report to a FINRA Facility for a previously executed trade for which a tape report has been submitted to the Facility, or for the offsetting portion of a riskless principal or agency transaction for which a non-tape, non-clearing report already has been submitted to the Facility satisfying FINRA regulatory requirements.¹⁰ In other words, the information contained in a clearing-only, non-regulatory report must be duplicative of information reported to the FINRA Facility in other submissions.

Pursuant to the proposed rule change, a clearing-only, non-regulatory report cannot be used to satisfy any regulatory reporting requirement under FINRA rules that may apply to the transaction, e.g., the identification of other members for agency or riskless principal transactions.¹¹ Thus, members will only be permitted to use such reports where the member’s regulatory reporting obligations have been satisfied through other reports (tape or non-tape, as applicable) submitted to the FINRA Facility. Submission of a clearing-only, non-regulatory report constitutes certification by the member that it has satisfied all regulatory reporting requirements that may apply to the transaction through its other submissions.

¹⁰ See, e.g., current Rules 7130(g)(1), 7230A(i)(1), 7230B(h)(1) and 7330(h)(1), which prohibit members from submitting to a FINRA Facility any non-tape report associated with a previously executed trade that was not reported to that FINRA Facility, except where submitting the offsetting portion of a riskless principal or agency transaction. See also Regulatory Notice 07-38 (August 2007).

¹¹ See Rules 6282(d)(4), 6380A(d)(4), 6380B(d)(4) and 6622(d)(4).

Members that opt to submit such reports would be required to use a unique indicator to denote that the report is submitted solely for purposes of clearing the transaction and not for purposes of satisfying any regulatory reporting requirements. If a clearing submission does not comply with the provisions of the Rule, e.g., if it is being used to satisfy any regulatory reporting requirements, then the member must not use the unique indicator. FINRA is proposing a conforming change to Rules 7130(d), 7230A(d), 7230B(d) and 7330(d), which identify the information that must be included in trade reports submitted to FINRA, to require members to append the unique indicator to denote a clearing-only, non-regulatory report, if applicable.

Although clearing-only, non-regulatory reports will not be used by members to satisfy their regulatory reporting obligations, the information contained in such reports must nonetheless be consistent with previously submitted information for the same transaction, unless otherwise expressly provided under FINRA rules. Thus, FINRA is also proposing to amend Rules 6160, 6170 and 6480 to expressly allow members that operate an ATS to use an MPID other than their ATS MPID on clearing-only, non-regulatory reports.¹² FINRA notes, however, that this relief relates solely to the MPID requirement, and the member firm with the trade reporting obligation under FINRA rules (or the “executing party”) must continue to be identified as such in all clearing-only, non-regulatory reports.

In addition, FINRA is proposing to amend Rules 7130(d), 7230A(d), 7230B(d) and 7330(d) to provide that members are not required to use the short sale (or short sale exempt) indicator, if applicable, on clearing-only, non-regulatory reports. The short sale indicator must be included on the required tape report and if submitted, non-tape non-clearing report that identifies

¹² If a member is using its clearing submission to satisfy any of its regulatory reporting obligations, then it must use its ATS MPID (and may not use its main broker-dealer MPID) in the clearing submission.

the FINRA member that is selling short (or short exempt). The member is not required to duplicate this information on the optional clearing-only, non-regulatory report.

FINRA reiterates that use of the clearing-only, non-regulatory report is not mandatory, and members will have the option of continuing to use clearing submissions to satisfy their regulatory reporting obligations. However, where a member opts to submit a clearing-only, non-regulatory report that duplicates trade information reported to FINRA in other tape and non-tape, non-clearing reports, then the member would be required to comply with the requirements set forth in this proposed rule change.

To further illustrate the application of the proposed rule change, FINRA is providing the following detailed example: Member Firm 1 operates an ATS that uses the MPID “MATS,” and Firm 1’s main broker-dealer MPID is “MOTH.” Firm 1 executes an agency cross transaction in its ATS between member Firm 2, as the buyer, and member Firm 3, as the seller. Under FINRA rules, using its ATS MPID “MATS,” Firm 1 must report the transaction to FINRA for public dissemination (for purposes of this example, “MATS” reports a cross transaction) and must submit non-tape report(s) to identify Firms 2 and 3 as parties to the trade, because they are FINRA members (“MATS” sells to Firm 2 and “MATS” buys from Firm 3). Firm 1 has the option, but is not required, to also report the transaction to FINRA for submission to clearing. Under the proposed rule change, Firm 1 could opt to submit two additional reports, i.e., two clearing-only, non-regulatory reports, with the unique indicator specified by FINRA, using an MPID other than its ATS MPID (“MOTH” sells to Firm 2 and “MOTH” buys from Firm 3). In making such submissions, per the terms of the proposed rule change, Firm 1 is certifying that it has satisfied all regulatory reporting requirements through the submission of the tape and non-tape, non-clearing reports. Alternatively, Firm 1 would have the option of designating the non-

tape reports showing “MATS” sells to Firm 2 and “MATS” buys from Firm 3 for clearing. In that instance, Firm 1 would not use the special indicator because the reports are also satisfying Firm 1’s reporting obligation under FINRA rules to identify Firms 2 and 3 as parties to the trade.

Finally, FINRA notes that while the proposed rule change has been prompted by issues involving ATS trade reporting, any FINRA member (e.g., a member that does not operate an ATS but nonetheless uses multiple MPIDs) could elect to use clearing-only, non-regulatory reports in accordance with the proposed rule change.

FINRA believes that the proposed rule change will ensure the accuracy and efficiency of FINRA’s audit trail and automated surveillance programs while accommodating firms’ business models and reporting and clearing processes that rely on clearing against their main broker-dealer MPID. The proposed rule change will ensure a more accurate audit trail by distinguishing voluntary trade reports that are submitted only to facilitate clearing from reports that are required under FINRA’s trade reporting rules to satisfy a member’s regulatory reporting obligations. Further, by distinguishing clearing-only, non-regulatory reports from other trade submissions, the proposed rule change will improve the efficiency of FINRA’s automated surveillance programs by potentially preventing false alerts that require both FINRA and member firms to unnecessarily expend resources to address such alerts.

FINRA has filed the proposed rule change for immediate effectiveness and proposes that the operative date will be in February 2016. FINRA will announce the operative date in a Regulatory Notice. To provide members sufficient time to make the required systems changes, FINRA expects to publish updated technical specifications for the FINRA Facilities at least four months prior to the operative date.

2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,¹³ 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 change is consistent with the Act because it will ensure a more accurate audit trail and enhance FINRA's ability to surveil on an automated basis for compliance with FINRA trade reporting 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.

Economic Impact Analysis

As described above, implementation of FINRA's reporting rules for ATSS creates an obligation for firms to report transactions to FINRA using an ATS-specific MPID. FINRA understands that requiring the submission of clearing reports with a firm's ATS-specific MPID would impose significant costs for firms with clearing processes that use their main broker-dealer MPID, and such a requirement would provide no material additional regulatory or market information beyond what is already provided through tape and non-tape regulatory reporting. Consequently, the proposed rule change is intended to remove a burden on firms that would provide no significant regulatory benefit if maintained.

While the proposed rule change would require some firms to implement systems changes to identify clearing-only, non-regulatory reports with a unique indicator, FINRA does not believe

¹³ 15 U.S.C. 78o-3(b)(6).

that these changes would impose significant or differential costs on similarly situated firms.¹⁴ Firms will not be required to submit clearing-only, non-regulatory reports and may continue to combine their regulatory reporting and clearing in the same report. Thus, firms will be free to select the method of reporting that best suits their business model. FINRA notes that firms would not be required to report consistently for all trades, i.e., a firm could submit clearing-only, non-regulatory reports for some trades, but not all.¹⁵ FINRA is proposing to provide members a sufficient implementation period to accommodate any such changes.

As noted above, the information in clearing-only, non-regulatory reports will be duplicative of information provided to FINRA in other reports. Accordingly, there will be no impact on the regulatory information that FINRA receives, and FINRA will be able to identify firms' use of clearing-only, non-regulatory reports in its audit trail. Therefore, the proposed rule change is not anticipated to create significant economic or informational impacts on the public, member firms or FINRA.

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;

¹⁴ FINRA notes that today, on average, approximately 350 members regularly report trades to the FINRA Facilities. Many firms, including smaller firms, route their order flow to another firm, e.g., their clearing firm, for execution, and as the routing firm, they do not have the trade reporting obligation. Thus, the proposed rule change will have no impact on many members.

¹⁵ FINRA further notes that firms would not be required to provide prior notice to FINRA of their intention to use clearing-only, non-regulatory reports.

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)(iii) of the Act¹⁶ and subparagraph (f)(6) of Rule 19b-4 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: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) 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-2015-035 on the subject line.

Paper comments:

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

¹⁶ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁷ 17 CFR 240.19b-4(f)(6).

All submissions should refer to File Number SR-FINRA-2015-035. 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 offices 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-2015-035, 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).