

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-76483; File No. SR-FINRA-2015-047)

November 19, 2015

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of a Proposed Rule Change to Adopt FINRA Rule 6191(a) to Implement the Quoting and Trading Requirements of the Regulation NMS Plan to Implement A Tick Size Pilot Program

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 November 13, 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. 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 FINRA Rule 6191 to implement the quoting and trading requirements of the Regulation NMS Plan to Implement a Tick Size Pilot Program (“Plan”).

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

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

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

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

On August 25, 2014, NYSE Group, Inc., on behalf of Financial Industry Regulatory Authority, Inc. (“FINRA”), BATS Exchange, Inc., BATS Y-Exchange, Inc., Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, the Nasdaq Stock Market LLC, New York Stock Exchange LLC (“NYSE”), NYSE MKT LLC, and NYSE Arca, Inc. (collectively “Participants”), filed with the Commission, pursuant to Section 11A of the Act<sup>3</sup> and Rule 608 of Regulation NMS thereunder, the Plan to implement a tick size pilot program (“Pilot”).<sup>4</sup> The Participants filed the Plan to comply with an order issued by the Commission on June 24, 2014.<sup>5</sup> The Plan<sup>6</sup> was published for comment in the Federal Register on November 7, 2014, and approved by the Commission, as modified, on May 6, 2015.<sup>7</sup>

The Plan is designed to allow the Commission, market participants, and the public to study and assess the impact of increment conventions on the liquidity and trading of the common

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<sup>3</sup> 15 U.S.C. 78k-1.

<sup>4</sup> See Letter from Brendon J. Weiss, Vice President, Intercontinental Exchange, Inc., to Secretary, Commission, dated August 25, 2014.

<sup>5</sup> See Securities Exchange Act Release No. 72460 (June 24, 2014), 79 FR 36840 (June 30, 2014).

<sup>6</sup> Unless otherwise specified, capitalized terms used in this rule filing are defined as set forth in the Plan. FINRA also proposes supplementary material as part of this proposed rule change to, among other things, provide that the terms used in proposed Rule 6191 shall have the same meaning as provided in the Plan, unless otherwise specified.

<sup>7</sup> See Securities Exchange Act Release No. 74892 (May 6, 2015), 80 FR 27514 (May 13, 2015) (“Approval Order”).

stocks of small-capitalization companies. Each Participant is required to comply with, and to enforce compliance by its members, as applicable, with the provisions of the Plan. As is described more fully below, the proposed rules would require members to comply with the applicable quoting and trading increments for Pilot Securities.<sup>8</sup>

The Pilot Securities will include stocks of companies with \$3 billion or less in market capitalization, an average daily trading volume of one million shares or less, and a volume weighted average price of at least \$2.00 for every trading day. The Pilot will consist of a Control Group of approximately 1400 Pilot Securities and three test groups with 400 Pilot Securities in each selected by a stratified sampling.<sup>9</sup> During the pilot, Pilot securities in the Control Group will be quoted and traded at the currently permissible increments. Pilot Securities in the first test group (“Test Group One”) will be quoted in \$0.05 minimum increments but will continue to trade at any price increment that is currently permitted.<sup>10</sup> Pilot Securities in the second test group (“Test Group Two”) will be quoted in \$0.05 minimum increments and will trade at \$0.05 minimum increments subject to a midpoint exception, a retail investor order exception, and a negotiated trade exception.<sup>11</sup> Pilot Securities in the third test group (“Test Group Three”) will be subject to the same restrictions as Test Group Two and also will be subject to the “Trade-at” requirement to prevent price matching by a market participant that is not displaying at the price of a Trading Center’s<sup>12</sup> “Best Protected Bid” or “Best Protected Offer,” unless an enumerated

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<sup>8</sup> Proposed Rule 6191 shall be in effect during a pilot period to coincide with the pilot period for the Plan (including any extensions to the pilot period for the Plan).

<sup>9</sup> See Section V of the Plan for identification of Pilot Securities, including criteria for selection and grouping.

<sup>10</sup> See Section VI(B) of the Plan.

<sup>11</sup> See Section VI(C) of the Plan.

<sup>12</sup> The Plan incorporates the definition of “Trading Center” from Rule 600(b)(78) of Regulation NMS. Regulation NMS defines a Trading Center as “a national securities

exception applies.<sup>13</sup> In addition to the exceptions provided under Test Group Two, an exception for Block Size orders and exceptions that mirror those under Rule 611 of Regulation NMS<sup>14</sup> apply to the Trade-at requirement.

Compliance with the Quoting and Trading Increments of the Plan

The Plan requires FINRA to establish, maintain, and enforce written policies and procedures that are reasonably designed to comply with applicable quoting and trading requirements specified in the Plan.<sup>15</sup> Accordingly, FINRA is proposing new Rule 6191 (Compliance with Regulation NMS Plan to Implement a Tick Size Pilot Program) to require members to comply with the Plan.

Proposed Rule 6191(a) (Compliance with Quoting and Trading Restrictions) (the “Rule”) sets forth the requirements for FINRA and FINRA members in meeting their quoting and trading obligations, as applicable, under the Plan. Rule 6191(a)(1) will require members to establish, maintain and enforce written policies and procedures that are reasonably designed to comply with the applicable quoting and trading requirements of the Plan. Rule 6191(a)(2) provides that FINRA systems will not display quotations in violation of the Plan and this Rule.

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exchange or national securities association that operates an SRO trading facility, an alternative trading system, an exchange market maker, an OTC market maker, or any other broker or dealer that executes orders internally by trading as principal or crossing orders as agent.”

<sup>13</sup> See Section VI(D) of the Plan.

<sup>14</sup> 17 CFR 242.611.

<sup>15</sup> FINRA is also required by the Plan to develop appropriate policies and procedures that provide for data collection and reporting to the Commission of data described in Appendixes B and C of the Plan. FINRA is separately proposing rules that would require compliance by FINRA members with the data collection and submission provisions of the Plan described in Section VII of the Plan, and has reserved Paragraph (b) for such rules.

Proposed Rule 6191(a)(3) clarifies the treatment of Pilot Securities that drop below \$1.00 during the Pilot Period. In particular, Rule 6191(a)(3) provides that, if the price of a Pilot Security drops below \$1.00 during regular trading hours on any trading day, such Pilot Security will continue to be a Pilot Security subject to the Plan. However, if the Closing Price of a Pilot Security on any given trading day is below \$1.00, such Pilot Security will be moved out of its Pilot Test Group into the Control Group, and may then be quoted and traded at any price increment that is currently permitted for the remainder of the Pilot Period. Rule 6191(a)(3) also provides that, notwithstanding anything contained within these rules to the contrary, Pilot Securities (whether in the Control Group or any Pilot Test Group) will continue to be subject to the data collection requirements of the Plan at all times during the Pilot Period and for the six-month period following the end of the Pilot Period.

In approving the Plan, the Commission noted that the Participants had proposed additional selection criteria to minimize the likelihood that securities that trade with a share price of \$1.00 or less would be included in the Pilot, and stated that, once established, the universe of Pilot Securities should stay as consistent as possible so that the analysis and data can be accurate throughout the Pilot Period.<sup>16</sup> FINRA notes that a Pilot Security that drops below \$1.00 during regular trading hours will remain in its applicable Test Group; a Pilot Security will only be moved to the Control Group if its Closing Price on any given trading day is below \$1.00. FINRA believes that this provision is appropriate because it will help ensure that Pilot Securities in Test Groups One, Two and Three continue to reflect the Pilot's selection criteria, helping ensure that they yield useful data. FINRA also believes that this provision is appropriate because

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<sup>16</sup> See Approval Order, *supra* note 7, 80 FR at 27535.

it responds to comments that the Plan address the treatment of securities that trade below \$1.00 during the Pilot Period.<sup>17</sup>

Proposed Rule 6191(a)(4) sets forth the applicable limitations for securities in Test Group One. Consistent with the language of the Plan, Rule 6191(a)(4) provides that no member may display, rank, or accept from any person any displayable or non-displayable bids or offers, orders, or indications of interest in any Pilot Security in Test Group One in increments other than \$0.05. However, orders priced to execute at the midpoint of the national best bid and national best offer (“NBBO”) or best protected bid and best protected offer (“PBBO”)<sup>18</sup> and orders entered in a Participant-operated retail liquidity program may be ranked and accepted in increments of less than \$0.05. Pilot Securities in Test Group One may continue to trade at any price increment that is currently permitted by applicable Participant, SEC and FINRA rules.

Proposed Rule 6191(a)(5) sets forth the applicable quoting and trading requirements for securities in Test Group Two. This provision states that no member may display, rank, or accept from any person any displayable or non-displayable bids or offers, orders, or indications of interest in any Pilot Security in Test Group Two in increments other than \$0.05. However,

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<sup>17</sup> See Approval Order, supra note 7, 80 FR at 27535. FINRA notes that this proposed change is also the subject of an application for exemptive relief from the Plan, filed pursuant to Rule 608(e) of Regulation NMS by NYSE on behalf of all the Participants. See Letter from Elizabeth K. King, NYSE, to Brent J. Fields, Secretary, Commission, dated October 14, 2015.

<sup>18</sup> Regulation NMS defines a protected bid or protected offer as a quotation in an NMS stock that (1) is displayed by an automated trading center; (2) is disseminated pursuant to an effective national market system plan; and (3) is an automated quotation that is the best bid or best offer of a national securities exchange, the best bid or best offer of The Nasdaq Stock Market, Inc., or the best bid or best offer of a national securities association other than the best bid or best offer of The Nasdaq Stock Market, Inc. See 17 CFR 242.600(57). In the Approval Order, the Commission noted that the protected quotation standard encompasses the aggregate of the most aggressively priced displayed liquidity on all Trading Centers, whereas the NBBO standard is limited to the single best order in the market. See Approval Order, supra note 7, 80 FR at 27539.

orders priced to execute at the midpoint of the NBBO or PBBO and orders entered in a Participant-operated retail liquidity program may be ranked and accepted in increments of less than \$0.05.

Proposed Rule 6191(a)(5) also sets forth the applicable trading restrictions for Test Group Two securities. Absent any of the exceptions listed in the Rule, no member may execute orders in any Pilot Security in Test Group Two in price increments other than \$0.05. The \$0.05 trading increment will apply to all trades, including Brokered Cross Trades.<sup>19</sup>

Consistent with the language of the Plan, the proposed Rule provides that Pilot Securities in Test Group Two may trade in increments of less than \$0.05 under the following circumstances: (1) trading may occur at the midpoint between the NBBO or the PBBO; (2) Retail Investor Orders may be provided with price improvement that is at least \$0.005 better than the PBBO; and (3) Negotiated Trades may trade in increments of less than \$0.05.

Proposed Rule 6191(a)(6) sets forth the applicable quoting and trading restrictions for Pilot Securities in Test Group Three. The proposed Rule provides that no member may display, rank, or accept from any person any displayable or non-displayable bids or offers, orders, or indications of interest in any Pilot Security in Test Group Three in increments other than \$0.05. However, orders priced to execute at the midpoint of the NBBO or PBBO and orders entered in a Participant-operated retail liquidity program may be ranked and accepted in increments of less than \$0.05. The rule also states that, absent any of the applicable exceptions, no member that operates a Trading Center may execute orders in any Pilot Security in Test Group Three in price

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<sup>19</sup> A brokered cross trade is a trade that a broker-dealer that is a member of a Participant executes directly by matching simultaneous buy and sell orders for a Pilot Security. See Section I(G) of the Plan.

increments other than \$0.05. The \$0.05 trading increment will apply to all trades, including Brokered Cross Trades.

Proposed Rule 6191(a)(6)(C) sets forth the exceptions pursuant to which Pilot Securities in Test Group Three may trade in increments of less than \$0.05. First, trading may occur at the midpoint between the NBBO or PBBO. Second, Retail Investor Orders may be provided with price improvement that is at least \$0.005 better than the PBBO. Third, Negotiated Trades may trade in increments of less than \$0.05.

Proposed Rule 6191(a)(6)(D) sets forth the “Trade-at Prohibition,” which is the prohibition against executions by a member that operates a Trading Center of a sell order for a Pilot Security in Test Group Three at the price of a Protected Bid or the execution of a buy order for a Pilot Security in Test Group Three at the price of a Protected Offer during regular trading hours, absent any of the exceptions set forth in Rule 6191(a)(6)(D). Consistent with the Plan, the proposed Rule reiterates that a member that operates a Trading Center that is displaying a quotation, via either a processor or an SRO quotation feed, that is at the price of a Protected Bid or Protected Offer is permitted to execute orders at that level, but only up to the amount of its displayed size. A member that operates a Trading Center that was not displaying a quotation that is the same price as a Protected Quotation, via either a processor or an SRO quotation feed, is prohibited from price-matching protected quotations unless an exception applies.

Consistent with the Plan, proposed Rule 6191(a)(6)(D) also sets forth the exceptions to the Trade-at prohibition, pursuant to which a member that operates a Trading Center may execute a sell order for a Pilot Security in Test Group Three at the price of a Protected Bid or execute a buy order for a Pilot Security in Test Group Three at the price of a Protected Offer. The first exception to the Trade-at Prohibition is the “display exception,” which allows a trade to

occur at the price of the Protected Quotation, up to the Trading Center’s full displayed size, if the order “is executed by a trading center that is displaying a quotation.”<sup>20</sup>

In Rule 6191(a)(6)(D), FINRA proposes that a member that utilizes the independent aggregation unit concept may satisfy the display exception only if the same independent aggregation unit that displays interest via either a processor or an SRO Quotation Feed also executes an order in reliance upon this exception. The rule provides that “independent aggregation unit” has the same meaning as provided under Rule 200(f) of SEC Regulation SHO.<sup>21</sup> This provision also recognizes that not all members may utilize the independent aggregation unit concept as part of their regulatory structure, and still permits such members to utilize the display exception if all the other requirements of that exception are met.

As initially proposed by the Participants, the Plan contained an additional condition to the display exception, which would have required that, where the quotation is displayed through a national securities exchange, the execution at the size of the order must occur against the displayed size on that national securities exchange; and where the quotation is displayed through the Alternative Display Facility or another facility approved by the Commission that does not provide execution functionality, the execution at the size of the order must occur against the displayed size in accordance with the rules of the Alternative Display Facility of such approved

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<sup>20</sup> See Section VI(D)(1) of the Plan.

<sup>21</sup> 17 CFR 242.200. Treatment as an independent aggregation unit is available if traders in an aggregation unit pursue only the particular trading objective(s) or strategy(ies) of that aggregation unit and do not coordinate that strategy with any other aggregation unit. Therefore, one independent aggregation unit within a Trading Center cannot execute trades pursuant to the display exception in reliance on quotations displayed by a different independent aggregation unit. As an example, an agency desk of a Trading Center cannot rely on the quotation of a proprietary desk in a separate independent aggregation unit at that same Trading Center.

facility (“venue limitation”).<sup>22</sup> Some commenters stated that this provision was anti-competitive, as it would have forced off-exchange Trading Centers to route orders to the venue on which the order was displayed.<sup>23</sup>

In approving the Plan, the Commission modified the Trade-At Prohibition to remove the venue limitation.<sup>24</sup> The Commission noted that the venue limitation was not prescribed in its Order mandating the filing of the Plan.<sup>25</sup> The Commission also noted that the venue limitation would have unnecessarily restricted the ability of off-exchange market participants to execute orders in Test Group Three Securities, and that removing the venue limitation should mitigate concerns about the cost and complexity of the Pilot by reducing the need for off-exchange Trading Centers to route to the exchange.<sup>26</sup> The Commission also stated that the venue limitation did not create any additional incentives to display liquidity in furtherance of the purposes of the Trade-At Prohibition, because the requirement that a Trading Center could only trade at a protected quotation up to its displayed size should be sufficient to incentivize displayed liquidity.<sup>27</sup>

Consistent with Plan and the SEC’s determination to remove the venue limitation, FINRA is making clear that the display exception applies to trades executed by a Trading Center otherwise than on an exchange where the Trading Center has previously displayed a quotation in either an agency, riskless principal or principal capacity. As part of the display exception,

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<sup>22</sup> See Securities Exchange Act Release No. 73511 (November 3, 2014), 79 FR 66423, 66437 (November 7, 2014).

<sup>23</sup> See Approval Order, supra note 7, 80 FR at 27540.

<sup>24</sup> See Approval Order, supra note 7, 80 FR at 27540.

<sup>25</sup> See Approval Order, supra note 7, 80 FR at 27540.

<sup>26</sup> See Approval Order, supra note 7, 80 FR at 27540.

<sup>27</sup> See Approval Order, supra note 7, 80 FR at 27540.

FINRA also proposes that a Trading Center that is displaying a quotation as agent or riskless principal may only execute as agent or riskless principal, while a Trading Center displaying a quotation as principal (excluding riskless principal) may execute either as principal or agent or riskless principal. FINRA believes this is consistent with the Plan and the objective of the Trade-at Prohibition, which is to promote the display of liquidity and generally to prevent any Trading Center that is not quoting from price-matching Protected Quotations. Providing that a Trading Center may not execute on a proprietary basis in reliance on a quotation representing customer interest (whether agency or riskless principal) ensures that the Trading Center cannot avoid compliance with the Trade-at Prohibition by trading on a proprietary basis in reliance on a quotation that does not represent such Trading Center's own interest. Where a Trading Center is displaying a quotation at the same price as a Protected Quotation in a proprietary capacity, transactions in any capacity at the price and up to the size of such Trading Center's displayed quotation would be permissible. Transactions executed pursuant to the display exception may occur on the venue on which such quotation is displayed or over the counter.

The proposal also excepts Block Size orders<sup>28</sup> and permits Trading Centers to trade at the price of a Protected Quotation, provided that the order is of Block Size at the time of origin and is not an aggregation of non-block orders, broken into orders smaller than Block Size prior to submitting the order to a Trading Center for execution; or executed on multiple Trading Centers.<sup>29</sup> The Plan only provides that Block Size orders shall be exempted from the Trade-At

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<sup>28</sup> "Block Size" is defined in the Plan as an order (1) of at least 5,000 shares or (2) for a quantity of stock having a market value of at least \$100,000.

<sup>29</sup> Once a Block Size order or portion of such Block Size order is routed from one Trading Center to another Trading Center in compliance with Rule 611 of Regulation NMS, the Block Size order would lose the proposed Trade-at exemption, unless the Block Size remaining after the first route and execution meets the Block Size definition under the Plan.

Prohibition. In requiring that the order be of Block Size at the time of origin and not an aggregation of non-block orders, or broken into orders smaller than Block Size prior to submitting the order to a Trading Center for execution; or executed on multiple Trading Centers, FINRA believes that it is providing clarity as to the circumstances under which a Block Size order will be excepted from the Trade-At Prohibition.

Consistent with the Plan, the proposal also excepts an order that is a Retail Investor Order that is executed with at least \$0.005 price improvement.

The exceptions set forth in proposed Rule 6191(a)(6)(D)(iii) d. through l. are based on the exceptions found in Rule 611 of Regulation NMS.<sup>30</sup> The subparagraph d. exception applies when the order is executed when the Trading Center displaying the Protected Quotation that was traded at was experiencing a failure, material delay, or malfunction of its systems or equipment. The subparagraph e. exception applies to an order that is executed as part of a transaction that was not a “regular way” contract. The subparagraph f. exception applies to an order that is executed as part of a single-priced opening, reopening, or closing transaction by the Trading Center. The subparagraph g. exception applies to an order that is executed when a Protected Bid was priced higher than a Protected Offer in a Pilot Security. The subparagraph h. exception applies when the order is identified as a Trade-at Intermarket Sweep Order. The subparagraph i. exception applies when the order is executed by a Trading Center that simultaneously routed Trade-at Intermarket Sweep Orders to execute against the full displayed size of the Protected Quotation that was traded at. The subparagraph j. exception applies when the order is executed as part of a Negotiated Trade. The subparagraph k. exception applies when the order is executed when the Trading Center displaying the Protected Quotation that was traded at had displayed,

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<sup>30</sup> See 17 CFR 242.611.

within one second prior to execution of the transaction that constituted the Trade-at, a Best Protected Bid or Best Protected Offer, as applicable, for the Pilot Security with a price that was inferior to the price of the Trade-at transaction.

The exception proposed in subparagraph l. applies to a “stopped order.” Both the Plan and Rule 6191(a)(6) define a “stopped order” as an order that is executed by a Trading Center which, at the time of order receipt, the Trading Center had guaranteed an execution at no worse than a specified price, where (1) the stopped order was for the account of a customer; (2) the customer agreed to the specified price on an order-by-order basis; and (3) the price of the Trade-at transaction was, for a stopped buy order, equal to the National Best Bid in the Pilot Security at the time of execution or, for a stopped sell order, equal to the National Best Offer in the Pilot Security at the time of execution.

Consistent with the Plan, the final exception to the Trade-At Prohibition and its accompanying supplementary material applies to an order that is for a fractional share of a Pilot Security. The supplementary material provides that such fractional share orders may not be the result of breaking an order for one or more whole shares of a Pilot Security into orders for fractional shares or that otherwise were effected to evade the requirements of the Trade-at Prohibition or any other provisions of the Plan. In approving the Plan, the Commission noted that this exception was appropriate, as there could be potential difficulty in the routing and executing of fractional shares.<sup>31</sup>

Rule 6191(a)(7) addresses the operation of certain exceptions to the Pilot. Rule 6191(a)(7)(A) relates to the Retail Investor Order exception. Consistent with the Plan, the proposed Rule defines a “Retail Investor Order” as an order that originates from a natural person,

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<sup>31</sup> See Approval Order, *supra* note 7, 80 FR at 27541.

provided that, prior to submission, no change is made to the terms of the order with respect to price or side of market and the order does not originate from a trading algorithm or any other computerized methodology.<sup>32</sup> A Retail Investor Order may be an odd lot, round lot, or partial round lot.

Proposed Rule 6191(a)(7)(A) addresses the execution of Retail Investor Orders other than on a national securities exchange. Given that the definition of a “Retail Investor Order” in the Plan includes that the order is an agency or riskless principal order, orders received directly from a customer, without an accompanying capacity, and executed by the receiving Trading Center would not currently fall within the scope of the Plan’s definition of “Retail Investor Order” and the corresponding exceptions from Test Groups Two and Three. FINRA is therefore proposing that any member that operates a Trading Center may execute against an order received directly from a natural person that did not originate from a trading algorithm or any other computerized methodology. This proposed provision generally tracks the Plan’s definition of “Retail Investor Order” while allowing a member to execute against orders received directly from retail customers.

The Plan also provides that the Trading Center executing a Retail Investor Order must sign an attestation that substantially all orders to be executed as Retail Investor Orders will qualify as such under the Plan. Rule 6191(a)(7)(A) provides that any member for which FINRA is the Designated Examining Authority (DEA) that operates a Trading Center and executes Retail Investor Orders must submit a signed attestation to FINRA that substantially all orders to be executed as Retail Investor Orders will qualify as such under this Rule.

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<sup>32</sup> See Section I(DD) of the Plan.

Finally, FINRA is proposing 6191(a)(7)(B) to clarify how members should report trades when utilizing one of the enumerated exceptions to the Trade-at requirement. Rule 6191(a)(7)(B) provides that a member that is relying on an exception to the Trade-at prohibition for a transaction otherwise than on a national securities exchange must include all applicable modifiers in trade reports pursuant to Rules 6282, 6380A and 6380B. This provision will facilitate the accurate and complete reporting of transactions in Pilot Securities by member.

If the Commission approves the proposed rule change, the proposed rule change will become operative on October 3, 2016.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>33</sup> 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, and Section 15A(b)(9) of the Act,<sup>34</sup> which requires that FINRA rules not impose any burden on competition that is not necessary or appropriate.

FINRA believes that this proposal is consistent with the Act because it implements and clarifies the provisions of the Plan, and is designed to assist FINRA and members in meeting regulatory obligations pursuant to the Plan. In approving the Plan, the SEC noted that the Pilot was an appropriate, data-driven test that was designed to evaluate the impact of a wider tick size on trading, liquidity, and the market quality of securities of smaller capitalization companies, and was therefore in furtherance of the purposes of the Act. To the extent that this proposal implements and clarifies the Plan and applies specific requirements to members, FINRA believes

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<sup>33</sup> 15 U.S.C. 78o-3(b)(6).

<sup>34</sup> 15 U.S.C. 78o-3(b)(9).

that this proposal is in furtherance of the objectives of the Plan, as identified by the SEC, and is therefore consistent with the Act.

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. FINRA notes that the proposed rule change implements the provisions of the Plan, and is designed to assist FINRA in meeting its regulatory obligations pursuant to the Plan. FINRA also notes that the quoting and trading requirements of the Plan will apply equally to all firms that trade Pilot Securities.

Economic Impact Assessment

Need for the Rule

As noted above, the Plan directs FINRA to establish rules and procedures for itself and member firms necessary in meeting their obligations under the Plan. The rules and procedures proposed here should be reasonably designed to allow the Commission, market participants, and the public to study and assess the impact of increment conventions on the liquidity and trading of the common stocks of small-capitalization companies.

The rule, as proposed here, essentially codifies the Plan as approved by the Commission. FINRA is proposing rules relating to the operation of the Plan, including provisions intended to modify the obligations and prohibitions of the Plan market participants in a manner that is consistent with the stated objectives of the Plan.

First, as discussed above, in Rule 6191(a)(6)(D), FINRA proposes to permit that a member that operates a Trading Center and chooses to use aggregation units may rely upon the display exception only with respect to a transaction executed at the price of a Protected

Quotation if the order is executed within the same independent aggregation unit that displayed a quotation that is equal in price to the Protected Quotation.

Second, as part of the display exception, FINRA also proposes to provide that a Trading Center that is displaying a quotation as agent or riskless principal may only execute as agent or riskless principal, while a Trading Center displaying a quotation as principal (excluding riskless principal) may execute either as principal or agent or riskless principal.

Third, under proposed Rule 6191(a)(7)(A), FINRA is proposing that any member that operates a Trading Center may execute against an order received directly from a natural person that did not originate from a trading algorithm or any other computerized methodology and continue to qualify for the Retail Investor Order exception.

#### Economic Baseline

The baseline used by FINRA to evaluate the impact of the proposed rule change is the regulatory framework under the Plan, specifically the Control Group consisting of securities that will be quoted and traded at the currently permissible increments. An additional baseline considered corresponds to the current regulatory framework, prior to the implementation of the Plan. These two baselines serve as the primary points of comparison for assessing economic impacts, including the incremental benefits and costs of the proposed rule.

Trading Centers currently can quote in the common stock of small and middle-capitalization companies at the minimum increment permissible by the SEC of \$0.01. In the Approval Order, the SEC identified concerns with decimalization, particularly with respect to the market quality for securities of small and middle-sized capitalization companies, such as the potential for reduced incentives to underwriters, limited sell-side research on these companies, and less market-making in these securities.

Under the Plan, all market participants who are active in Pilot Securities will quote and trade securities in the Pilot Test Groups in the manner prescribed by the Plan. The conditions for each Test Group are discussed above. All market participants that will participate in the Pilot by virtue of their activity in Pilot Securities will have established the functionality within their systems to trade and quote at the permissible increments, as well as update the set of securities in each Test Group on a daily basis.

#### Economic Impacts

The analysis of economic impacts focuses on the instances where the proposed rule modifies requirements to the Plan as adopted.

#### Anticipated Benefits

##### The Display Exception

As noted above, proposed Rule 6191(a)(6)(D) would limit the ability of a Trading Center operated by a member that chooses to use independent aggregation units to avail itself of the display exception only with respect to a transaction executed at the price of a Protected Quotation if the order is executed within the same independent aggregation unit that displayed the Protected Quotation. This clarification would enhance the incentives of any independent aggregation unit to provide liquidity under the Plan.

In its absence, all independent aggregation units of the same trading center could conceivably take advantage of the display exception when any one unit were to post a quotation that meets the exception, in essence creating an opportunity for related aggregation units to “free ride” on the eligible quotation. Thus, the proposal may promote displayed liquidity by aggregation units that are active in Pilot Securities in Test Group 3, which would be consistent with the objectives of the Pilot.

### Capacity of the Orders Displayed

The second proposal requires that the Trading Center in taking advantage of a trade exception provided by the Plan, must act as agent or riskless principal if the quotation that provides the exception is an agency or riskless principal quotation. In its absence, a trading center could conceivably execute proprietary trades on its own behalf even when it is not providing the additional liquidity through a quotation representing its own interest, in essence possibly allowing a Trading Center to avoid displaying proprietary interest while still availing itself of the exception. By facilitating the display of liquidity representing the Trading Center's capital commitment, the proposal may facilitate the goals of the Pilot.

### Definition of Retail Investor Order

The third proposal extends the definition of Retail Investor Order to include any order received directly from a natural person that did not originate from a trading algorithm or any other computerized methodology, without requiring that such order be an agency or riskless principal order.

In the absence of this change, many orders that are currently sent to Trading Centers that otherwise satisfy the Retail Order definition would not be eligible for the exceptions of the Plan in the OTC market solely due to the capacity (or lack thereof) of that order. Retail customers could avail themselves of the exemption by placing additional conditions on the order, but this might preclude some Trading Centers from being able to interact with these orders. Therefore, this may provide greater liquidity to Test Group Two and Three Pilot Securities.

### Anticipated Costs

#### The Display Exception

Under the clarification proposed, independent aggregation units not displaying quotations are not covered by the exception. Members that operate Trading Centers that utilize multiple independent aggregation units may be disadvantaged compared to members that operate Trading Centers with a single independent aggregation unit, or members that do not utilize aggregation units. But this impact may be small, as there is no prohibition from multiple independent aggregation units providing quotations covered by the exceptions. Thus all are eligible to take advantage of the exceptions provide under the Plan.

#### Capacity of the Order Displayed

Trading Centers would be limited in their capacity to transact under FINRA's proposed exception to this rule. Some orders that would be able to trade under the exception as set forth in the Plan would no longer be eligible. These orders may thus have a lower probability of execution and potentially worse execution quality, if executed. It is difficult to assess the extent to which this might occur prior to the Pilot, but the data collected by the Plan will permit an analysis of this potential impact.

#### Definition of Retail Investor Order

To the extent that this clarification creates added competition by Trading Centers to provide executions under the exceptions of the Plan, some Trading Centers may lose order flow to trading centers that would not have been permitted to execute these trades but for the clarification. FINRA notes that others may gain from this increase in competition, so that the overall effect could be beneficial.

#### 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

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be 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](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2015-047 on the subject line.

##### Paper Comments:

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

All submissions should refer to File Number SR-FINRA-2015-047. 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 a.m. and 3 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 Number SR-FINRA-2015-047 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>35</sup>

Brent J. Fields  
Secretary

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<sup>35</sup> 17 CFR 200.30-3(a)(12).