

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-86178; File No. SR-FINRA-2019-014)

June 21, 2019

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change to Allow Additional Time for Reporting to TRACE of Transactions in U.S. Treasury Securities Executed to Hedge a Primary Market Transaction

I. Introduction

On April 16, 2019, 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 FINRA Rule 6730 to provide additional time for reporting to TRACE of transactions in U.S. Treasury Securities executed to hedge a primary market transaction. The proposed rule change was published for comment in the Federal Register on April 30, 2019.<sup>3</sup> On June 13, 2019, pursuant to Section 19(b)(2) of the Act,<sup>4</sup> the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change.<sup>5</sup> The Commission received one comment letter in support of the proposed rule change.<sup>6</sup> This order approves the proposed rule change.

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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. 85713 (April 24, 2019), 84 FR 18329 (April 30, 2019) (“Notice”).

<sup>4</sup> 15 U.S.C. 78s(b)(2).

<sup>5</sup> See Securities Exchange Act Release No. 86101 (June 13, 2019), 84 FR 28601 (June 19, 2019) (designating July 29, 2019, as the date by which the Commission shall approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to approve or disapprove the proposed rule change).

## II. Description of the Proposal

Currently, a transaction in a U.S. Treasury Security executed on a business day up to 5:00 p.m. E.T. must be reported on the same day during TRACE System Hours.<sup>7</sup> For a transaction in a U.S. Treasury Security executed on a business day after 5:00 p.m. E.T., a member must report the trade no later than the next business day (T+1) during TRACE System Hours, and, if reported on T+1, the member must designate the trade “as/of” and include the date of execution.<sup>8</sup>

According to FINRA, institutional investors often hedge a primary market transaction that meets the definition of “List or Fixed Offering Price Transaction” or “Takedown Transaction” (i.e., a “P1” transaction) with a U.S. Treasury Security.<sup>9</sup> In such cases, hedges in U.S. Treasury Securities and the P1 transactions are executed in close time proximity because the desired hedge position in the U.S. Treasury Security cannot be determined until the underwriters complete pricing of P1 issue and make allocations to customers.<sup>10</sup> Once pricing is complete for

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<sup>6</sup> See Letter from Robert Toomey, Managing Director and Associate General Counsel, SIFMA, to Robert W. Errett, Deputy Security, Commission, dated May 21, 2019 (“SIFMA Letter”).

<sup>7</sup> See FINRA Rule 6730(a)(4)(A)(i). FINRA Rule 6710(t) defines “TRACE System Hours” to mean “the hours the TRACE system is open, which are 8:00:00 a.m. Eastern Time through 6:29:59 p.m. Eastern Time on a business day, unless otherwise announced by FINRA.”

<sup>8</sup> See FINRA Rule 6730(a)(4)(A)(ii).

<sup>9</sup> FINRA Rule 6710(q) and (r) define “List or Fixed Offering Price Transactions” and “Takedown Transactions,” which are identified with the “P1” modifier, generally as primary market sale transactions on the first day of trading of a security: (i) by a sole underwriter, syndicate manager, syndicate member or selling group member at the published or stated list or fixed offering price (or, for Takedown Transactions, at a discount from the published or stated list or fixed offering price) or (ii) in the case of primary market sale transactions effected pursuant to Securities Act Rule 144A, by an initial purchaser, syndicate manager, syndicate member or selling group member at the published or stated fixed offering price (or, for Takedown Transactions, at a discount from the published or stated fixed offering price).

<sup>10</sup> See Notice, 84 FR at 18330.

the new issue, any associated hedging trades in U.S. Treasury Securities must be entered and reported to TRACE.<sup>11</sup> Under current FINRA Rule 6730, a trade report for a transaction in a U.S. Treasury Security executed by 5:00 p.m. ET is due on trade date (by the close of TRACE System Hours), whereas a P1 trade report is due on T+1 (by the close of TRACE System Hours).<sup>12</sup>

FINRA understands that this difference in TRACE reporting timeframes for the hedging transactions in U.S. Treasury Securities and the related P1 transaction can present operational challenges for members, particularly where pricing of the debt new issue occurs prior to, but near, 5:00 p.m. E.T.<sup>13</sup> In response to these concerns, FINRA has proposed to align the TRACE reporting timeframe for any hedging transactions in U.S. Treasury Securities associated with a P1 transaction with the deadline for reporting the related P1 transaction. Specifically, FINRA has proposed to amend FINRA Rule 6730 to provide that a transaction in a U.S. Treasury Security executed to hedge a P1 transaction must be reported no later than the next business day (T+1) during TRACE System Hours and, if reported on T+1, designated “as/of” and include the date of execution.<sup>14</sup> FINRA also proposed that a member must append a new trade modifier when reporting to TRACE any transaction in a U.S. Treasury Security that is executed to hedge a P1 transaction.<sup>15</sup>

FINRA has stated that it will announce the effective date of the rule change in a Regulatory Notice to be published no later than 90 days following a Commission approval, and the effective date will be no later than 270 days following publication of that Regulatory

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<sup>11</sup> See id.

<sup>12</sup> See FINRA Rule 6730(a)(2) and (4).

<sup>13</sup> See Notice, 84 FR at 18330.

<sup>14</sup> See proposed FINRA Rule 6730(a)(4)(B).

<sup>15</sup> See proposed FINRA Rule 6730(d)(4)(G)(iii).

Notice.<sup>16</sup>

### III. Discussion and Commission Findings

After careful consideration, 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>17</sup> In particular, the Commission finds that the proposed rule change is consistent with Section 15A(b)(6) of the Act,<sup>18</sup> which requires, among other things, that FINRA rules 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. The Commission believes that aligning the reporting deadline for U.S. Treasury Security hedge transactions with the deadline for the associated P1 transaction is reasonably designed to minimize compliance burdens on FINRA members who report to TRACE without adversely impacting regulatory surveillance. In addition, because P1 transactions and transactions in U.S. Treasury Securities are not subject to public dissemination, the rule change would not negatively impact market transparency. The new requirement to flag any transaction in a U.S. Treasury Security used to hedge a P1 transaction is reasonably designed to enhance the TRACE audit trail, consistent with the protection of investors and the public interest. The Commission notes that the one comment letter received on the proposal was supportive.<sup>19</sup>

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<sup>16</sup> See Notice, 84 FR at 18330.

<sup>17</sup> In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>18</sup> 15 U.S.C. 78o-3(b)(6).

<sup>19</sup> See SIFMA Letter, supra note 6 (opining that the proposal would “ease the operational burden on member firms, provide a better characterization of the transaction for market surveillance purposes through the linkage that will be reported, and result in fewer late Treasury transaction filings to the TRACE system”).

Pursuant to Section 19(b)(5) of the Act,<sup>20</sup> the Commission consulted with and considered the views of the Treasury Department in determining to approve the proposed rule change. The Treasury Department indicated its support for the proposal.<sup>21</sup> Pursuant to Section 19(b)(6) of the Act,<sup>22</sup> the Commission has considered the sufficiency and appropriateness of existing laws and rules applicable to government securities brokers, government securities dealers, and their associated persons in approving the proposal. As discussed above, by aligning the TRACE reporting timeframe for transactions in U.S. Treasury Securities executed to hedge a P1 transaction with the deadline for reporting the related P1 transaction, and adopting a new modifier to identify such transactions, the proposed rule change is reasonably designed to minimize burdens on FINRA members who must report to TRACE without adversely impacting regulatory surveillance or market transparency.

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<sup>20</sup> 15 U.S.C. 78s(b)(5) (providing that the Commission “shall consult with and consider the views of the Secretary of the Treasury prior to approving a proposed rule filed by a registered securities association that primarily concerns conduct related to transactions in government securities, except where the Commission determines that an emergency exists requiring expeditious or summary action and publishes its reasons therefor”).

<sup>21</sup> E-mail from Treasury Department staff to Michael Gaw, Assistant Director, Division of Trading and Markets, Commission (June 17, 2019).

<sup>22</sup> 15 U.S.C. 78s(b)(6).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>23</sup> that the proposed rule change (SR-FINRA-2019-014) is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>24</sup>

Jill M. Peterson  
Assistant Secretary

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<sup>23</sup> 15 U.S.C. 78s(b)(2).

<sup>24</sup> 17 CFR 200.30-3(a)(12).