

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-93966; File No. SR-FINRA-2021-029)

January 12, 2022

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Order Approving Proposed Rule Change to Amend FINRA Rule 6732 and Expand the Scope of Exemptions that FINRA May Grant ATSS from the TRACE Reporting Requirements

I. Introduction

On November 15, 2021, 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”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend FINRA Rule 6732 (Exemption from Trade Reporting Obligation for Certain Transactions on an Alternative Trading System) to expand the scope of exemptions from the transaction reporting obligations of FINRA Rule 6730 (Transaction Reporting) that FINRA may grant to a member alternative trading system (“ATS”). The proposed rule change was published for comment in the Federal Register on November 30, 2021.³ The Commission received no comments on the proposed rule change. This order approves the proposed rule change.

II. Description of the Proposal

FINRA Rule 6730(a) requires each FINRA member that is a Party to a Transaction in a TRACE-Eligible Security⁴ to report the transaction to the Trade Reporting and Compliance

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 93651 (November 23, 2021), 86 FR 67996 (November 30, 2021) (“Notice”).

⁴ See FINRA Rule 6710(a) (defining “TRACE-Eligible Security”).

Engine (“TRACE”). FINRA Rule 6710(e) defines “Party to a Transaction” as an introducing broker-dealer (if any), an executing broker-dealer, or a customer. An alternative trading system (“ATS”) is a Party to a Transaction occurring through its system and has a TRACE transaction reporting obligation, unless an exception or exemption applies.⁵

FINRA Rule 6732 provides FINRA with the authority to exempt a member ATS from TRACE reporting obligations under FINRA Rule 6730. FINRA has stated that it adopted Rule 6732 in response to concerns raised by members regarding operational difficulties arising from the reporting of certain transactions on an ATS, particularly when the ATS does not have a role in the clearance and settlement for trades on its system.⁶ If FINRA grants an ATS an exemption under Rule 6732, a member subscriber of the ATS, when engaging in a trade on the ATS covered by the Rule 6732 exemption, must report against its counterparty (rather than the ATS), which mitigates these operational difficulties and facilitates clearance and settlement.⁷

Currently, under Rule 6732, FINRA may grant an ATS an exemption if the following criteria are satisfied: (1) a trade is between two FINRA members; (2) the trade does not pass through any ATS account, and the ATS seeking the exemption does not exchange TRACE-Eligible Securities or funds on behalf of the subscribers or take either side of the trade for clearing or settlement purposes, or in any other way insert itself into the trade; (3) the ATS

⁵ See Regulatory Notice 14-53 (November 2014).

⁶ See Notice, 86 FR at 67997. FINRA explained that members’ back-end systems are often programmed to clear against the counterparty identified on TRACE trade reports, and when the ATS is not involved in clearance and settlement, member subscribers often prefer to TRACE-report against the party with which they clear and settle the trade (i.e., another subscriber, rather than the ATS). See id.

⁷ See id.

seeking the exemption agrees to provide data relating to each exempted trade to FINRA on either a monthly basis or as otherwise proscribed by FINRA, and acknowledges that failure to meet this requirement would result in its exemption being revoked; (4) the ATS seeking the exemption pays the applicable reporting fee to FINRA; and (5) the ATS seeking the exemption has entered into a written agreement with each member that is a Party to a Transaction to ensure that each exempted trade is properly reported.⁸ Where these criteria are satisfied, an exempted trade occurring on the ATS must be reported by a member (other than the ATS) that meets the definition of “Party to a Transaction” identifying a counterparty other than the ATS with respect to each side of the trade.⁹

FINRA is now proposing to amend Rule 6732 to expand the scope of transactions that may be exempted under Rule 6732 to include trades that involve only one FINRA member (other than the ATS). Specifically, FINRA proposes to delete the current language in subparagraph (a)(1) of Rule 6732 that requires an exempted transaction to be between two FINRA members, and replace it with the following: “The trade involves at least one member (other than the ATS) that meets the definition of ‘Party to a Transaction.’”

FINRA has stated that, in many cases, transactions on an ATS that involve only one member are otherwise similar to the transactions between two members that are currently eligible for exemptive relief under existing Rule 6732.¹⁰ FINRA believes that expanding the scope of the current exemption to permit its use for transactions between a member (other than the ATS) and a non-member subscriber would extend the benefits of the rule—including

⁸ See FINRA Rule 6732(a).

⁹ See FINRA Rule 6732(b).

¹⁰ See Notice, 86 FR at 67997.

simplifying compliance with TRACE trade reporting obligations—for additional ATS models and member subscribers, while capturing substantially the same regulatory information and enabling public dissemination of the transaction in a more streamlined manner.¹¹

FINRA also has proposed to add new paragraph (c) to Rule 6732, which provides that, with respect to a transaction between a member and a non-member on an ATS that is a “covered ATS,”¹² the ATS must provide to the member subscriber, and the member subscriber must report to TRACE using, the FINRA-assigned identifier for each non-FINRA member subscriber.

FINRA also has stated that an ATS that has received an exemption under Rule 6732 and that is a “covered ATS” must use the FINRA-assigned identifier to identify each non-FINRA member subscriber in the monthly transaction files that are required to be submitted to FINRA.¹³

FINRA has represented that it will announce the effective date of the rule change in a Regulatory Notice, and the effective date will be no later than 365 days following Commission approval of the proposed rule change.¹⁴

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

¹¹ See id.

¹² See FINRA Rule 6730.07 (defining “covered ATS” as an ATS “that executed transactions in U.S. Treasury Securities against non-FINRA member subscribers of \$10 billion or more in monthly par value, computed by aggregating buy and sell transactions, for any two months in the preceding calendar quarter”).

¹³ See Notice, 86 FR at 67998, n. 12.

¹⁴ See Notice, 86 FR at 67998.

a national securities association.¹⁵ In particular, the Commission finds that the proposed rule change is consistent with Section 15A(b)(6) of the Act,¹⁶ which requires, among other things, that the rules of a national securities association 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 proposed rule change appears reasonably designed to reduce reporting burdens on member ATSS and to mitigate operational burdens of ATS member subscribers with respect to clearance and settlement, without negatively impacting the regulatory audit trail or post-trade transparency for ATS transactions in TRACE-Eligible Securities. The proposed rule change will expand the scope of existing Rule 6732 by allowing FINRA to grant exemptions from the TRACE reporting requirements to ATSS regarding member-to-non-member trades in addition to, as currently, member-to-member trades. The proposal does not change any of the other criteria for granting an exemption under Rule 6732.

Thus, although an ATS receiving an exemption pursuant to FINRA's expanded authority under Rule 6732 would no longer be submitting TRACE reports regarding exempted trades, the proposal appears reasonably designed to prevent any relevant information regarding such trades from being lost from the regulatory audit trail. An ATS granted an exemption under FINRA's expanded authority would have to enter into a written agreement with each member subscriber that is a Party to a Transaction that is exempted, specifying that the member must report that transaction to TRACE and identify the transaction as having occurred on the ATS using the

¹⁵ 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).

¹⁶ 15 U.S.C. 78o-3(b)(6).

ATS's MPID.¹⁷ The sole member subscriber involved in the transaction would have to identify a counterparty other than the ATS with respect to each side of the transaction.¹⁸ In addition, an ATS granted an exemption would have to agree to provide FINRA on a monthly basis (or such other basis as prescribed by FINRA) data relating to exempted trades occurring on the ATS's system, and to acknowledge that failure to report such data to FINRA, in addition to constituting a violation of FINRA rules, would result in revocation of any exemption granted pursuant to Rule 6732.¹⁹ Furthermore, under new Rule 6732(c), for an exempted trade between a member and a non-member on an ATS that is a "covered ATS" under FINRA Rule 6730.07, the ATS would have to provide to the member subscriber (and the member subscriber would have to report to TRACE using) the FINRA-assigned identifier for each non-FINRA member subscriber.

The proposal also appears reasonably designed to prevent any negative impact on post-trade transparency. Although trade reports for exempt trades will no longer be submitted by the ATS and publicly disseminated, market observers will still have relevant information about the ATS trade between the member subscriber and the non-member because FINRA will continue to publicly disseminate the trade report submitted by the member subscriber that is the Party to the Transaction. This approach aligns public dissemination more closely with the legal and economic effects of the transaction, because an exemption under Rule 6732 can apply to a trade on the ATS only if the broker-dealer operator of the ATS is not a legal counterparty to the trade.²⁰

¹⁷ See FINRA Rule 6732(a)(5).

¹⁸ See FINRA Rule 6732(b).

¹⁹ See FINRA Rule 6732(a)(3).

²⁰ See FINRA Rule 6732(a)(2).

For the reasons noted above, the Commission finds that the proposed rule change is consistent with the Act.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²¹ that the proposed rule change (SR-FINRA-2021-029) is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²²

J. Matthew DeLesDernier
Assistant Secretary

²¹ 15 U.S.C. 78s(b)(2).

²² 17 CFR 200.30-3(a)(12).