

November 15, 2007

Barbara Z. Sweeney  
Office of the Corporate Secretary  
FINRA  
1735 K Street, NW  
Washington, D.C. 20006-1506

Re: Regulatory Notice 07-46: Proposed Amendments to OTC  
Trade Reporting Requirements for Equity Securities

Dear Ms. Sweeney:

UBS Securities LLC (“UBS”) respectfully submits this comment letter concerning the Financial Industry Regulatory Authority’s (“FINRA”) proposed amendments to the over-the-counter (“OTC”) trade reporting requirements for equity securities, as discussed in Regulatory Notice 07-46.<sup>1</sup> First and foremost, UBS wishes to emphasize its support for an executing broker-dealer reporting structure whereby the broker-dealer executing a trade between member firms would always have the trade reporting obligation. Furthermore, UBS does not necessarily oppose FINRA’s proposal to require broker-dealers to provide information linking related trade reports when both a tape and non-tape report are submitted to FINRA for the same overall transaction. However, we strongly believe that the linking information should be reported through a system other than ACT and at the end of the day instead of on a real time or intra-day basis. Specifically, UBS proposes a reporting mechanism that would link tape and non-tape trade reports using information reported into the Order Audit Trail System (“OATS”).

## **I. Trade Reporting Structure Proposal**

### Current Reporting Structure

Under current NASD Rules, the following trade reporting structure requires that: (1) in transactions between two market makers, the sell-side reports the trade; (2) in transactions between a market maker and a non-market maker, the market maker reports the trade; (3) in transactions between non-market makers, the sell-side reports the trade; and (4) in transactions between a member firm and either a non-member firm or customer, the member firm reports the trade.<sup>2</sup> As FINRA noted in

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<sup>1</sup> See FINRA Regulatory Notice 07-46, OTC Trade Reporting (Sept. 2007).

<sup>2</sup> See NASD Rules 4632(b); 4632A(b); 4632C(b); 4632E(b); and 6620(b).

Regulatory Notice 07-46, the current reporting structure can result in confusion, delays, and double-reporting, as the parties to a trade attempt to determine which party has the trade reporting obligation.<sup>3</sup> In addition, the recent implementation of Rule 611 of Regulation NMS has further complicated the current trade reporting structure.<sup>4</sup>

### Regulation NMS Implications

Pursuant to NASD Rules, member firms are required to include appropriate modifiers when submitting trade reports to denote when a certain exception or exemption to Rule 611 is being used.<sup>5</sup> However, in a transaction where the broker-dealer responsible for reporting the trade is not the executing broker-dealer, the trade reporting firm will generally not know whether the executing broker-dealer relied upon an exception or exemption from Rule 611.

For example, Market Maker A routes a sell order to Market Maker B. Market Maker B executes the order at a price outside the National Best Bid and Offer ("NBBO") and routes intermarket sweep orders in compliance with Rule 611(b)(6).<sup>6</sup> Market Maker B promptly sends an execution report to Market Maker A. Under the current reporting structure, Market Maker A has the trade reporting obligation since it is the seller. However, Market Maker A would be unaware of whether Market Maker B, as the executing broker-dealer, relied on the intermarket sweep order exception to Rule 611. Consequently, Market Maker A reports the trade with an execution price inferior to the NBBO without including the proper Regulation NMS modifier. These types of situations result in inaccurate trade reports submitted to ACT and an increase in the number of false positive trade-throughs that appear on the Consolidated Tape.

### Executing Broker-Dealer Reporting Structure

UBS believes that a new reporting structure that requires the executing broker-dealer to report trades between two member firms is the most logical and effective solution to the above mentioned quandary. Specifically, the executing broker-dealer knows the material terms and details of the transaction, as well as any Rule 611 exceptions or exemptions that apply to the trade. Accordingly, the executing broker-dealer is in the best position to report the trade in a timely manner with the appropriate Regulation NMS modifier, if applicable.

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<sup>3</sup> Regulatory Notice 07-46 at 3.

<sup>4</sup> 17 CFR §242.611.

<sup>5</sup> NASD Rule 4632(a); *see also* FINRA Notice to Members 07-23, NASD Trade Reporting Requirements Related to Regulation NMS (May 2007).

<sup>6</sup> 17 CFR § 242.611(b)(6)

In implementing an executing broker-dealer reporting structure, it is imperative to clearly identify which party to a trade is the executing broker-dealer. UBS believes that for transactions between two member firms that involve the routing of electronic orders, the executing broker-dealer should be the firm that receives the order for handling and execution. However, with regard to transactions between two member firms where it is more difficult to determine which is the executing broker-dealer, such as trades negotiated over the telephone between two market makers, UBS proposes that the current trade reporting structure should apply. In today's markets, we believe that the number of telephone negotiated trades between broker-dealers is relatively small compared to transactions involving the routing of electronic orders.

In the event FINRA decides to implement an executing broker-dealer reporting structure, UBS will require sufficient time to reprogram its trade reporting systems. UBS will require approximately nine (9) to twelve (12) months from the time that final changes to the Trade Reporting Facility systems are implemented to make corresponding modifications to its own systems.

## **II. Linking Proposal**

### *Proposed Linking Requirement*

FINRA is proposing to require member firms to provide information sufficient to link tape and non-tape trade reports that are submitted to FINRA for the same overall transaction.<sup>7</sup> Under current NASD Rules, member firms are not required to provide such information when reporting trades.

As stated earlier, UBS does not necessarily oppose FINRA's proposal for requiring member firms to provide information that would link tape and non-tape trade report submissions. However, UBS does not believe that the linking information provided by the member firms should be reported through ACT. Due to the immense amount of quotation traffic caused by increased automation in the securities markets and the implementation of Regulation NMS, UBS's order handling and execution systems are required to process an enormous amount of information and data at incredible speeds to comply with regulatory obligations. Our systems are further burdened by the complex and sometimes duplicative trade reporting requirements imposed by the FINRA Rules. Requiring member firms to provide additional information through ACT to link multiple trade submissions would only increase the complexity, redundancy, and delays of the current trade reporting process and impose additional burdens on order handling and execution systems.

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<sup>7</sup> Regulatory Notice 07-46 at 4.

UBS is also concerned that FINRA's linking proposal for riskless principal trades may conflict with other regulatory requirements. For example, the FINRA proposal may not conform to the NYSE's recent amendments to Rule 92 concerning riskless principal trade reporting to its Front End Systematic Capture ("FESC") system. If there are significant differences between the FESC trade reporting requirements and FINRA's proposed linking rules, UBS will have to devote substantial time and resources to modify its systems to accommodate both regulatory requirements.

In addition to the above, UBS has several concerns with any proposal that would require member firms to submit linking information on a real time or intra-day basis. One area of concern is that a UBS trader may not always know at the time of executing an order whether, or what portion of, the order ultimately will be deemed executed on a riskless principal basis. This dilemma makes it extremely difficult for us to identify a trade as riskless principal in order to append an appropriate identifier on a real time basis. Furthermore, in situations where UBS accumulates a position through multiple street-side trades and then transfers the accumulated position to a customer on a riskless principal basis, it will be unduly burdensome to develop and implement a system that could link the street-side trades with the customer trade using an identifier on a real time or intra-day basis.

#### *Proposal to Link Multiple Trade Reports Using OATS Data*

As an alternative to FINRA's proposal, UBS proposes an end-of-day reporting mechanism to link tape and non-tape trade submissions using data reported to OATS. FINRA created OATS as an integrated audit trail of order event information which is used to recreate events in the life cycle of orders and to monitor the trading practices of member firms. The linking of tape and non-tape reports appears to fall within the scope of OATS reporting. Where real-time trade reporting is necessary for transparency and risk management, audit trail information is best handled at the end of the day. Relatively minor amendments to the OATS technical specifications would provide FINRA with a reasonable method to link all related tape and non-tape trade events while at the same time removing the possibility of delayed trade reports. UBS proposes the formation of an industry panel, potentially through the SIFMA Trading Committee, to evaluate and propose an OATS solution to the linking proposal.

In the event FINRA decides to implement a process for linking tape and non-tape trade reports submitted for the same overall transaction, UBS will require sufficient time to reprogram its trade reporting systems. UBS will require approximately nine (9) to twelve (12) months from the time that final changes to the Trade Reporting Facility systems are implemented to make corresponding modifications to its own systems.

### III. Conclusion

UBS appreciates this opportunity to address the issues raised by FINRA's proposed amendments to the OTC trade reporting requirements. We believe that an executing broker-dealer reporting structure with specially tailored rules for telephone negotiated trades is the most logical and effective way to streamline the trade reporting process, reduce inaccurate reports, and address the issues resulting from the implementation of Regulation NMS. Furthermore, UBS maintains that the linking of tape and non-tape trade reports related to the same overall transaction should be accomplished through an end-of-day reporting mechanism that uses data reported into OATS. Subject to the specific comments set forth above, we support FINRA's efforts and welcome the opportunity to respond to any questions that may arise from our views expressed in this letter. Please direct any inquiries to our Compliance Department, attention Scott W. Anderson, at 203-719-5620.

Sincerely,



Joseph Mecane  
Managing Director  
Chairman, Market Structure Committee