Regulatory Notice 09-21

Trade Reporting

FINRA Adopts Amendments Relating to Reporting Transfers of Proprietary Positions in Debt and Equity Securities in Connection With Certain Corporate Control Transactions

Effective Date: May 4, 2009

April 2009

Notice Type

- Rule Amendment

Suggested Routing

- Compliance
- Executive Representatives
- Legal
- Operations
- Senior Management
- Systems
- Trading
- Training

Key Topic(s)

- Alternative Display Facility
- NMS Stocks
- OTC Equity Securities
- OTC Reporting Facility
- Trade Reporting and Compliance Engine
- Trade Reporting
- Trade Reporting Facilities

Referenced Rules & Notices

- FINRA Rule 6282
- FINRA Rule 6380A
- FINRA Rule 6380B
- FINRA Rule 6622
- FINRA Rule 6750
- FINRA Rule 7130
- FINRA Rule 7230A
- FINRA Rule 7230B
- FINRA Rule 7330
- Schedule A to the FINRA By-Laws

Executive Summary

Effective May 4, 2009, firms are not required to report to FINRA for purposes of publication transfers of proprietary positions in debt and equity securities between a member firm and another member firm or non-member broker-dealer under certain specific conditions, as outlined in this *Notice*.

The text of the amendments can be found at *www.finra.org/rulefilings/2009-024*.

Questions regarding this *Notice* may be directed to:

- The Legal Section, Market Regulation, at (240) 386-5126; or
- The Office of General Counsel at (202) 728-8071.

Background and Discussion

Description of Trade Reporting Exception

On April 3, 2009, FINRA filed with the SEC a proposed rule change for immediate effectiveness to adopt a limited exception to the trade reporting rules.[1] Specifically, firms are not required to report to FINRA for purposes of publication transfers of proprietary positions in debt and equity securities between a member firm and another member firm or non-member broker-dealer under the following conditions.

Financial Industry Regulatory Authority

- First, the transfer must be effected in connection with a merger of one firm with the other firm or a direct or indirect acquisition of one firm by the other firm or the other firm's parent company.
- Second, the transfer must not be in furtherance of a trading or investment strategy.

While such transfers are not reportable for publication purposes under the amended rules, firms nonetheless must report them to FINRA for regulatory purposes and for purposes of assessing applicable regulatory transaction fees pursuant to Section 3 of Schedule A to the FINRA By-Laws and/or trading activity fees under Section 1(b) of Schedule A to the FINRA By-Laws.[2]

To qualify for the exception, the position transfer must be effected as part of an overall sale and the consolidation of the firms' separate proprietary trading businesses. A position transfer driven by a trading or investment strategy does not qualify for the exception and must be reported for publication purposes. For example, as a result of a corporate control transaction, Firm 1 (a member firm) acquires all of the assets of Firm 2 (another member firm or non-member broker-dealer), or Firm 1's parent company acquires Firm 2, such that Firm 1 and Firm 2 become wholly owned by the same parent company. In connection with the corporate control transaction, Firm 1 and Firm 2 consolidate their separate sales and trading businesses onto a single platform and, along with the migration of sales and trading personnel, clients and systems and technology, Firm 2's proprietary positions are transferred to Firm 1. In this instance, the transfer from Firm 2 to Firm 1 would fall within the trade reporting exception and would not be reportable for publication purposes, but must be reported to FINRA for regulatory purposes.

By way of further example, Firm 1 (a member firm) and Firm 2 (another member firm or non-member broker-dealer) currently are wholly owned by the same parent company and operate separately. Firm 1 owns 100,000 shares of ABCD security and the value of ABCD has increased substantially since Firm 1 purchased the shares. As part of an investment strategy, Firm 1 sells the shares to Firm 2. In this instance, the sale from Firm 1 to Firm 2 would not fall within the trade reporting exception and must be reported to FINRA for publication purposes.

The trade reporting exception is expressly limited to transfers of proprietary positions that are effected in connection with a merger or a direct or indirect acquisition between two member firms or a member firm and a non-member broker-dealer only. FINRA notes that these corporate control transactions are among the changes in a firm's ownership or control that would trigger the notice requirements and membership application process under FINRA rules. Thus, the trade reporting exception generally applies where the merger or acquisition would require the firm to submit notice and/or an application under FINRA rules. However, because FINRA membership application rules are broader than the scope of this trade reporting exception, FINRA is clarifying that the exception will *not* be considered satisfied merely because a firm has submitted an application or notice under FINRA membership rules.

Specific Reporting Requirements

Firms must provide FINRA written notice of their intent to use this exception, including the basis for their determination that the transfer meets the terms of the exception, at least three business days in advance of the transfer. Such notice should be sent to FINRA's Market Regulation Department:

- via email at *tradereporting@finra.org*; or
- via regular mail at:

  FINRA
  Market Regulation Department
  Attn: Director of Trade Reporting
  9509 Key West Avenue
  Rockville, MD 20850

Notifying FINRA in advance does not constitute approval by FINRA of the transaction as properly qualifying under the terms of the exception. Rather, a firm relying on the exception must ensure that a given transfer satisfies the terms of the exception, and the firm's advance written notice of the transfer to FINRA does not constitute an estoppel as to FINRA or otherwise bind FINRA in any subsequent administrative, civil or disciplinary proceeding with respect to a firm's misuse of the exception.

Under the amended rules, firms are required to report the transfer in the manner prescribed by FINRA and must designate that the reports are submitted for regulatory and not publication purposes. For transfers of equity securities positions, firms must submit a non-tape (either non-tape, non-clearing or clearing-only) report and, until further notice,[3] shall append the unique modifier (.RA) used to denote "away from the market sales." Firms should note that FINRA does not consider transfers that qualify under the trade reporting exception described in this *Notice* to be "away from the market sales" (even if the value assigned to the transferred securities is not at the prevailing market price). By requiring firms to use the .RA modifier in this instance, FINRA is not in any way expanding its narrow interpretation of the "away from the market sales" trade reporting exception.[4] For transfers of debt positions, firms are required to use a special value of "T" in the capacity field of the trade report. Firms must first request that FINRA Operations enable their reporting Market Participant Symbol (MPID) for position transfer entry by contacting FINRA Operations at (866) 776-0800 or *FINRAOperations@finra.org*. Firms also should refer to the applicable technical specifications for the FINRA facility to which they are reporting trades.

Firms generally should report to FINRA on the same day as the ultimate transfer of the positions on their books and records, unless later reporting is warranted under specific circumstances. FINRA expects that in most instances, if firms cannot report on the same day that the transfers are reflected on their books and records (*e.g.*, if the transfers take place after the close of the FINRA trade reporting facilities), firms will report no later than the following business day (T+1). However, FINRA recognizes that for some transfers, manual processing may be required or other operational issues may arise.

The amendments are operative on Monday, May 4, 2009.

Endnotes

1 *See* Securities Exchange Act Release No. 59713 (April 6, 2009), 74 FR 17271 (April 14, 2009) (notice of filing and immediate effectiveness of SR-FINRA-2009-024).

2 *See* Rules 6282(i)(2) and 7130(c) relating to the Alternative Display Facility; 6380A(e)(2) and 7230A(g) relating to the FINRA/NASDAQ Trade Reporting Facility; 6380B(e)(2) and 7230B(f) relating to the FINRA/NYSE Trade Reporting Facility; 6622 and 7330(g) relating to the OTC Reporting Facility; and 6750(b) relating to the Trade Reporting and Compliance Engine.

3 Ultimately, a new unique modifier will be implemented specifically for use in connection with transfers reported pursuant to the trade reporting exception described in this *Notice*. FINRA will announce the new modifier in a *Trade Reporting Notice* and will provide firms sufficient time to make any necessary systems changes.

4 *See, e.g.*, Trade Reporting Frequently Asked Questions, Section 601 (Away from the Market Sales), available at *www.finra.org/Industry/Regulation/Guidance/P038942*.