Regulatory Notice 13-19

Trade Reporting

SEC Approves Amendments to Require Firms to Report OTC Transactions in Equity Securities as Soon as Practicable, But No Later Than 10 Seconds, Following Execution

Effective Date: November 4, 2013

Executive Summary

Effective Monday, November 4, 2013, firms are required to report over-the-counter transactions in equity securities[1] to FINRA as soon as practicable, but no later than 10 seconds, following execution. With respect to trades that are reported manually, FINRA will take into consideration the complexity and manual nature of the execution and reporting of the trade when reviewing for firm compliance with the new reporting time frame. The amendments also apply to trade cancellations, as well as stop stock and prior reference price trades.

The amended rule text is available at *www.finra.org/notices/13-19*.

Questions regarding this *Notice* may be directed to:

- Market Regulation, Legal Section, at (240) 386-5126;
- FINRA Operations at (866) 776-0800; or
- Office of General Counsel at (202) 728-8071.

Background and Discussion

The SEC recently approved amendments to the FINRA trade reporting rules regarding the time frame in which firms must report over-the-counter (OTC) transactions in equity securities executed during the hours that the FINRA trade reporting facilities are open.[2] Under the amendments, such transactions must be reported to FINRA as soon as practicable, but no later than 10 seconds, following execution.[3] In addition, the cancellation of trades executed during normal market hours and canceled during normal market hours on the date of execution must be reported as soon as practicable, but no later

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Notice Type

- Rule Amendment

Suggested Routing

- Compliance
- Legal
- Operations
- Senior Management
- Systems
- Trading

Key Topics

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

Referenced Rules & Notices

- FINRA Rule 6181
- FINRA Rule 6282
- FINRA Rule 6380A
- FINRA Rule 6380B
- FINRA Rule 6622
- FINRA Rule 6623
- FINRA Rule 7130
- FINRA Rule 7230A
- FINRA Rule 7230B

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than 10 seconds, after the time of cancellation.[4] Trades not reported within 10 seconds of execution, unless expressly subject to a different reporting requirement[5] or excluded from the trade reporting rules altogether, are late, and such trades are not considered "last sale" eligible under the Consolidated Tape Association Plan (CTA Plan) and Nasdaq Unlisted Trading Privileges Plan (UTP Plan).[6]

New Supplementary Material in FINRA Rules 6282, 6380A, 6380B and 6622 clarifies the requirement that firms report trades and trade cancellations "as soon as practicable." Firms must adopt policies and procedures reasonably designed to comply with this requirement and must implement systems that commence the trade reporting process without delay upon execution (or cancellation, as applicable). Where a firm has such reasonably designed policies, procedures and systems in place, the firm generally would not be viewed as violating the "as soon as practicable" requirement because of delays in trade reporting due to extrinsic factors that are not reasonably predictable and where the firm does not purposely intend to delay the reporting of the trade (*e.g.,* TRF systems issues). Firms must not purposely withhold trade reports, *e.g.,* by programming their systems to delay reporting until the last permissible second.

With respect to the 10-second reporting requirement, FINRA will continue to look for a pattern or practice of unexcused late trade reporting before taking action against a firm. Pursuant to Rules 6181 and 6623, unexcused late reporting occurs when there are "repeated reports of executions submitted after the required time period without reasonable justification or exceptional circumstances." The rules also provide that "[e]xceptional circumstances will be determined on a case-by-case basis and may include instances of system failure by a member or service bureau, or unusual market conditions, such as extreme volatility in a security, or in the market as a whole."[7] Firms that engage in a pattern or practice of unexcused late reporting (*i.e.,* reporting later than 10 seconds after execution) may be charged with violating FINRA rules, notwithstanding that they have policies and procedures that contemplate commencing the trade reporting process without delay.

FINRA believes that firms should automate their trade reporting processes to the greatest extent possible, consistent with their trading style used to provide best execution to customers, and where automation is not feasible, they should implement more efficient trade entry processes to meet the 10-second reporting requirement. FINRA expects that firms will periodically assess their systems and processes to ensure that they have implemented the most efficient policies and procedures for timely trade reporting.

Manual Trade Reporting

FINRA recognizes that there is a small universe of trades for which the trade details must be entered manually. For these trades, the trade reporting process might not be completed within 10 seconds following execution, even where the firm has established efficient reporting processes and commences to report the trade without delay. Accordingly, new Supplementary Material in Rules 6282, 6380A, 6380B and 6622 provides that in these cases, FINRA will take such factors as the complexity and manual nature of the execution and reporting of the trade into consideration in determining whether "reasonable justification" exists to excuse what otherwise may be deemed to be a pattern or practice of late trade reporting. Among other things, FINRA will consider the complexity of a trade (*e.g.,* a volume-weighted average trade or an options-related trade) and size of a trade (*e.g.,* a trade that involves a basket of securities), as well as the fact that some amount of time must elapse between the commencement of the manual trade reporting process and the reporting of the trade. The Supplementary Material applies only where the details of a trade must be manually entered or typed into a trade reporting system following execution. Firms must maintain, and provide upon request, documentation sufficient to demonstrate that a trade was reported late due to the manual nature of the trade entry process following execution.

The amendments are effective on Monday, November 4, 2013.

Endnotes

1. Specifically, these are OTC transactions in (1) NMS stocks, which are reported through the Alternative Display Facility (ADF) or a Trade Reporting Facility (TRF); and (2) OTC equity securities (*i.e.,* non-NMS stocks such as OTC Bulletin Board securities), which are reported through the OTC Reporting Facility (ORF).

2. *See* Securities Exchange Act Release No. 69561 (May 13, 2013), 78 FR 29190 (May 17, 2013) (Order Approving the Proposed Rule Change, as Modified by Amendment No. 1; File No. SR-FINRA-2013-013).

3. *See* FINRA Rules 6282(a), 6380A(a), 6380B(a) and 6622(a).

4. *See* FINRA Rules 6282(a); 6380A(a) and (g); 6380B(a) and (f); 6622(a) and (f); 7130(b); 7230A(b); 7230B(b); and 7330(b).

   Conforming changes also were made to replace the reference to 30 seconds with 10 seconds in the rules relating to the reporting of stop stock and prior reference price transactions. *See* FINRA Rules 6282(a)(4)(F) and (G), 6380A(a)(5)(F) and (G), 6380B(a)(5)(F) and (G), and 6622(a)(5)(F) and (G).

5. For example, the amendments do not apply to the reporting requirements applicable to transactions in restricted equity securities, as defined in Rule 6420, effected under Securities Act Rule 144A, which transactions currently are subject to end of day reporting. *See* Rule 6622(a)(3).

6. Trades reported for public dissemination purposes are transmitted to three “tapes” based on the listing venue of the security: New York Stock Exchange securities (Tape A), NYSE Arca, NYSE MKT and other regional exchange securities (Tape B), and Nasdaq Stock Market securities (Tape C). Tape A and Tape B are governed by the CTA Plan and Tape C is governed by the UTP Plan.

7. FINRA notes that firms are expected to have sufficiently robust systems with adequate capacity to enable them to report within the time frame prescribed by FINRA rules. This includes periods of high volume that are regularly occurring or expected, such as market open and close, or where a firm is reporting a large basket of securities. Thus, for example, absent extraordinary circumstances or reasonable justification, a pattern or practice of late trade reporting at market open generally would not be considered “excused” under FINRA rules.