

Alternative Display Facility

SEC Approves Amendments to FINRA Rules 6271 and 6272 Regarding the Requirements For Firms Seeking Registration as FINRA Alternative Display Facility (ADF) Market Participants

Effective Date: February 3, 2014

Executive Summary

The Securities and Exchange Commission (SEC) has approved amendments to FINRA rules governing registration in and participation on the ADF. The amendments add new requirements to the application that prospective ADF market participants must submit to FINRA prior to submitting quotes on and reporting trades to the ADF. As part of the application process, the amendments require prospective ADF market participants to submit a deposit (ADF Deposit Amount) into escrow. The amendments also set forth the framework pursuant to which an ADF market participant may earn back some or all of its ADF Deposit Amount, enumerate additional documents that a firm seeking registration as an ADF market participant must execute, and clarify the process by which a firm's registration as an ADF market participant becomes effective.

The text of the new rule is available in the online FINRA Manual.

Questions concerning this *Notice* or FINRA Rules 6271 and 6272 should be directed to:

- ▶ Chris Stone, Vice President, Transparency Services, at (202) 728-8457;
- ▶ Brendan Loonam, Director – Business Services, Transparency Services, at (212) 858-4203;
- ▶ Brant Brown, Associate General Counsel, Office of General Counsel (OGC), at (202) 728-6927; or
- ▶ Andrew Madar, Associate General Counsel, OGC, at (202) 728-8071.

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Notice Type

- ▶ Rule Amendment

Suggested Routing

- ▶ Compliance
- ▶ Legal
- ▶ Operations
- ▶ Senior Management

Key Topics

- ▶ Alternative Display Facility

Referenced Rules & Notices

- ▶ FINRA Rule 6271
- ▶ FINRA Rule 6272

Discussion

The ADF is a quotation collection and trade reporting facility that provides ADF market participants (*i.e.*, ADF-registered market makers or electronic communications networks (ECN)) the ability to post quotations, display orders and report transactions in NMS stocks for submission to Securities Information Processors for consolidation and dissemination to vendors and other market participants.¹ In connection with migrating the ADF to FINRA's Multi Product Platform (MPP), FINRA is amending the rules governing the operation of the ADF to add new registration requirements for prospective ADF market participants and to clarify the procedure by which an ADF market participant's registration becomes effective.

FINRA Rule 6271 currently requires that a firm seeking registration as an ADF market participant (either as a market maker or as an ECN) file an application with FINRA that, among other things, certifies the firm's good standing with FINRA, and demonstrates the firm's compliance with the net capital provisions of the Securities Exchange Act. FINRA has amended Rule 6271 to include additional items as part of a firm's application. Specifically, the firm must agree to submit an ADF Deposit Amount of \$250,000 in five equal installments into escrow. If the firm requests that FINRA accelerate the migration of the ADF to the MPP, or if the firm begins quoting on or reporting trades to the ADF within 90 calendar days after an ADF market participant that requested accelerated migration of the ADF begins quoting on and reporting trades to the ADF, the ADF Deposit Amount is \$500,000. The firm also must agree to the ADF deposit terms, which are set forth in greater detail in the rule. As part of the revised application, the firm must also agree that, for the two-year period following the effective date of its registration, failing to submit 75 percent of its quoting and trading volume to the ADF will result in the forfeiture of some or all of its ADF Deposit Amount, pursuant to the ADF deposit terms. Finally, the firm agrees to provide FINRA with reasonable monthly projections of the volume of data that it anticipates submitting to the ADF.

Rule 6271 also provides a framework through which an ADF market participant can earn back some or all of its ADF Deposit Amount through a credit structure based on the market data revenue associated with the firm's trade reporting activity on the ADF. The rule also addresses the treatment of the ADF Deposit Amount in the event the firm is sold, goes out of business, otherwise does not meet its obligations or fails to complete the process for becoming an ADF market participant. Finally, the rule provides for the release of a portion of the ADF Deposit Amount in the event that FINRA is unable to make the ADF available to a firm after a specified period of time.

FINRA has also amended Rule 6271 to require that firms seeking registration as ADF market participants submit two other items in addition to the application. Specifically, a firm seeking registration as an ADF market participant must execute a Participant Agreement with FINRA at least six months prior, or such other shorter time period as may

be designated by FINRA, to quoting on or reporting trades to the ADF. The firm must also execute a Certification Record, pursuant to which it certifies its ability to comply with certain requirements of Regulation NMS.

FINRA also clarified the process by which a firm's registration as an ADF market participant becomes effective. Specifically, FINRA and the firm must execute both the firm's application to become an ADF market participant and the Participant Agreement. Additionally, the firm must execute the Certification Record, and the firm must receive a notice of approval from FINRA in the designated security types specified in its application.

Endnote

1. Rule 600 of Regulation NMS defines a protected bid or offer as a "quotation in an NMS stock that (1) is displayed by an automated trading center; (2) is disseminated pursuant to an effective national market system plan; and (3) is an automated quotation that is the best bid or best offer of a national securities exchange, the best bid or best offer of The Nasdaq Stock Market, Inc., or the best bid or best offer of a national securities association other than the best bid or best offer of The Nasdaq Stock Market, Inc." See 17 CFR 242.600(b)(57). As such, the best bid or offer for a stock that is displayed on the ADF would constitute a protected bid or offer under Regulation NMS.