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February 20, 2015

Via Electronic Mail (pubcom@finra.org)

Marcia E. Asquith
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA Regulatory Notice 14-46: Proposal to Identify OTC Equity Trades Reported More Than Two Seconds after Execution as "Out of Sequence" and Not Last Sale Eligible

Dear Ms. Asquith:

The Securities Industry and Financial Markets Association ("SIFMA")[1] submits this letter to comment on the above-referenced Regulatory Notice published by the Financial Industry Regulatory Authority ("FINRA"). In the Regulatory Notice, FINRA requests comment on a proposal to identify over-the-counter ("OTC") trades reported more than two seconds following trade execution as "out of sequence" and not last sale eligible for public dissemination purposes. The proposal is one of seven FINRA initiatives relating to equity market structure and automated trading activities.

For many years, SIFMA and its members have been vocal advocates and thought leaders on equity market structure issues. The U.S. equity markets are the deepest, most liquid and most efficient in the world, with investors enjoying extraordinarily low transaction costs, narrow spreads, and fast execution speeds. Nevertheless, SIFMA believes there are aspects of market structure that could be enhanced through steps designed to decrease unnecessary market complexity, increase transparency of market information, and promote fairness in access. To sharpen the focus on these important issues, SIFMA's Board of Directors convened a broad-based task force in 2014 of members from across the country and across the industry, including retail and institutional dealers and asset managers, to develop a series of tangible and actionable market structure reforms. Through this task force, SIFMA has developed more than a dozen specific recommendations for addressing equity market structure.[2]

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[1] The Securities Industry and Financial Markets Association (SIFMA) brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

[2] *See* SIFMA Equity Market Structure Recommendations (July 10, 2014), available at http://www.sifma.org/workarea/downloadasset.aspx?id=8589949840

SIFMA appreciates and supports FINRA's efforts to increase the accuracy of public trade reporting, consistent with our recommendations on transparency. However, the proposal raises questions that FINRA should clarify before this initiative is filed with the Securities and Exchange Commission ("SEC") as a proposed rule change. The questions fall into two areas. First, we have questions about the mechanics of the proposed two-second rule. Second, we request clarification about FINRA's interpretation of the "as soon as practicable" under its trade reporting rules.

I. Two-Second Rule for Determining Trades Out-of-Sequence

Under FINRA's current trade reporting rules, OTC trades in NMS stocks that are executed during the hours that a FINRA facility is open, must be reported as soon as practicable, but no later than 10 seconds, following trade execution.[3] Trades that are reported more than 10 seconds following execution are designated as "late" and are not last sale eligible.[4] In the Regulatory Notice, FINRA proposes to identify OTC trades in NMS stocks reported more than two seconds following trade execution as "out of sequence" and not last sale eligible for public dissemination purposes.[5] However, OTC trades reported more than two seconds, but less than 10 seconds, after execution would not be considered "late" under FINRA rules.[6]

SIFMA supports a two-second threshold for determining that a trade is out of sequence, but we believe that FINRA should not establish its own unique mechanism separate from the trade reporting mechanisms operated by the Securities Information Processors ("SIPs"). The issue of whether a trade is reported in a timely manner for purposes of FINRA rules is only part of the broader issue of whether the collective trades in NMS stocks (both OTC and exchange) are properly sequenced when they are published by the SIPs to market data recipients. Certainly, we agree that the reliability of the transaction reporting stream is enhanced when the likelihood of out of sequence trades is reduced. However, the issue of identifying and reporting out-of-sequence should be addressed consistently across all markets, not simply through the requirements of FINRA trade reporting facilities.

Instead of making its own out-of-sequence determination for OTC trades, FINRA should report both reporting time and execution time for OTC trades to the SIPs. The SIPs should then make market-wide determinations if transactions are out of sequence by comparing the incoming transaction's execution time against the execution time of the most recent transaction that was last sale eligible and published. FINRA and the SIPs should work together to incorporate the necessary functionality as part of the SIPs' current efforts to expand the message header formats

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[3] *See* FINRA Rule 6380A.

[4] *Id.*

[5] *See* FINRA Regulation Notice 14-46.

[6] *Id.*

to include participant timestamps.[7] This approach will enhance and improve market data for all market participants.[8]

In addition, any proposal on identifying and reporting out of sequence trades should take into account the trading characteristics of thinly-traded stocks. FINRA states in the Regulatory Notice that it considered whether to create a separate construct for thinly-traded stocks but decided not to do so. However, FINRA does not address how it would treat a trade reported more than two seconds after execution where there were no other trades reported during that two second period. Under FINRA's proposal, that situation would lead to a trade being excluded from last sale calculations, thus resulting in market participants incorrectly believing there is no trading activity in the underlying security. Moving the out-of-sequence determinations to the SIPs would address that concern because the SIPs would be in the best position to compare OTC trades to exchange trades to make an overall determination of whether a trade should in fact be excluded from last sale eligibility.

II. Clarification Requested Regarding the Commencement of Reporting Trade Information to FINRA

SIFMA requests clarification on FINRA's proposal to amend Rule 6380A.02, which provides guidance on the requirements under Rule 6380A(a) and 6380A(g) to report trades and trade cancellations "as soon as practicable." Under the proposal, FINRA would add the following language to Supplementary Material .02:

> FINRA also interprets "as soon as practicable" to require members to disseminate trade information to other market participants no sooner than executed trade information is reported to FINRA for dissemination purposes.

In the Regulatory Notice, FINRA provides two specific examples of how it would interpret the "as soon as practicable" requirement:

- First, FINRA states that "an ATS cannot commence the process of disseminating trade information to its subscribers any faster than it commences the process of reporting the trade to FINRA for dissemination purposes."

[7] The expanded message headers will allow data recipients to identify the difference between the SIP's output timestamp and the timestamp provided by a participant when trades and quotes are submitted. *See, e.g.*, https://www.ctaplan.com/cta/popup/news/2513.

[8] As stated in SEC Chair White's June 5th, 2014 speech ("Enhancing Our Equity Market Structure"), it is particularly important that FINRA pass through the execution time stamp to the SIPs in order for industry participants to be able to better monitor the latency of the consolidated feeds. *See* http://www.sec.gov/News/Speech/Detail/Speech/1370542004312#.VONrE_nF8bg.

- Second, FINRA states that the "as soon as practicable" requirement "would prohibit an ATS from reporting back execution information to the subscriber on whose behalf the trade was executed sooner than it reports the information to FINRA."

The proposed amendment and the accompanying discussion in the Regulatory Notice raise questions about how to determine when trade information is considered *reported to* FINRA and at what point an ATS may *commence the process of* disseminating trade information to its subscribers.[9] In this regard, FINRA should clarify that a member firm would be in compliance with the "as soon as practicable" requirement if it sends trade information to FINRA and its subscribers contemporaneously, even if FINRA and the subscribers receive the information at different times. In addition, FINRA should clarify that delivery of information to any FINRA Trade Reporting Facility ("TRF") or to the FINRA Alternative Display Facility ("ADF") is considered to be delivery to FINRA for purposes of FINRA's trade reporting requirements and that member firms are not required to take into account any latency in delivery from the TRFs or the ADF to FINRA itself.

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SIFMA would be pleased to discuss these comments in further detail. If you have any questions, please contact either me (at 202-962-7383 or tlazo@sifma.org) or Timothy Cummings (at 212-313-1239 or tcummings@sifma.org).

Sincerely,

Theodore R. Lazo
Managing Director and
Associate General Counsel

cc: Stephanie Dumont/FINRA

[9] *See* FINRA Regulation Notice 14-46 at 5.