



8011-01p  
SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-67427; File No. SR- FINRA-2012-034)

July 12, 2012

Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend TRACE Reporting Rules Relating to Transfers of TRACE-Eligible Securities to Create or Redeem Instruments such as ETFs

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on July 11, 2012, Financial Industry Regulatory Authority, Inc. (“FINRA”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change, as described in Items I, II, and III below, which Items have been prepared by FINRA. FINRA has designated the proposed rule change as constituting a “non-controversial” rule change under paragraph (f)(6) of Rule 19b-4 under the Act,<sup>3</sup> which renders the proposal effective upon receipt of this filing by the Commission. The Commission is publishing this notice to solicit comment on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

FINRA is proposing to amend FINRA Rule 6730(e) to expressly exclude from the Trade Reporting and Compliance Engine (“TRACE”) trade reporting requirements transfers of TRACE-Eligible Securities for the sole purpose of creating or redeeming instruments such as exchange-traded funds (“ETFs”).

---

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 17 CFR 240.19b-4(f)(6).

The text of the proposed rule change is available on FINRA's website at <http://www.finra.org>, at the principal office of FINRA, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, FINRA included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. FINRA has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

A. Self-Regulatory Organization's Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

Under the Rule 6700 Series (the TRACE rules), members are required to report transactions in debt securities that are TRACE-Eligible Securities as defined in Rule 6710(a) to FINRA unless they fall within an express exception listed in Rule 6730(e). Certain transactions and transfers are not reported to FINRA (e.g., trades executed and reported through an exchange and transfers made pursuant to an asset purchase agreement that has been approved by a bankruptcy court). Members must have policies and procedures and internal controls in place to determine whether a transaction qualifies for an exception under the TRACE rules.

FINRA proposes to amend Rule 6730(e) to provide that transfers of TRACE-Eligible Securities for the sole purpose of creating or redeeming an instrument that evidences ownership or otherwise tracks the underlying securities transferred, such as an ETF, shall be excluded expressly from the TRACE reporting requirements. The proposed amendment to Rule 6730(e) is

similar to an exclusion for such transfers in equity securities incorporated in FINRA equity trade reporting rules in 2011.<sup>4</sup>

For example, a member broker-dealer that is an “authorized participant” of an ETF on behalf of a customer transfers TRACE-Eligible Securities to an ETF and in return receives ETF creation units. Under the proposed rule change, the transfers of the TRACE-Eligible Securities from the broker-dealer to the ETF would not be reported to TRACE.<sup>5</sup> (Similarly, the transfer of the ETF creation units to the broker-dealer would not be reported.)

In contrast, FINRA notes that purchases and sales of TRACE-Eligible Securities that are to be transferred for the purposes of creating or redeeming instruments such as ETFs (or a creation unit thereof) and subsequent purchases and sales of the ETF or a similar instrument in the secondary market are not subject to an exclusion. Such purchases and sales involving TRACE-Eligible Securities must be reported to FINRA in accordance with the Rule 6700 Series.

---

<sup>4</sup> See Securities Exchange Act Release No. 65025 (August 3, 2011), 76 FR 48937 (August 9, 2011) (SEC order approving SR-FINRA-2011-027, amending FINRA Rules 6282(i)(1), 6380A(e)(1), 6380B (e)(1) and 6622(e)(1)) and Regulatory Notice 11-40 (August 2011) (2011 Equity Trade Reporting Filing). The proposed rule change also codifies interpretive guidance that was published in 2003 regarding transfers of TRACE-Eligible Securities for such purposes. See Letter dated March 18, 2003, to Alice Yau, Vice President, Compliance, J.P. Morgan Securities from Sharon Zackula, Office of General Counsel, FINRA (f/k/a the National Association of Securities Dealers).

<sup>5</sup> FINRA notes that the proposed exception would apply irrespective of whether the member is acting as agent, principal or riskless principal in the creation process. Thus, if the broker-dealer that is an authorized participant in the above example is acting as riskless principal on behalf of its customer, the immediate subsequent transfer of the ETF creation units from the authorized participant to its customer also would not be reportable. Similarly, if a broker-dealer that is an authorized participant is acting as riskless principal on behalf of a customer that redeems an ETF creation unit, neither the transfer of the ETF creation unit from the broker-dealer to the ETF in return for TRACE-Eligible Securities, nor the immediate subsequent transfer of such TRACE-Eligible Securities to the customer would be reportable. This is consistent with interpretive guidance relating to the 2011 Equity Trade Reporting Filing. See Regulatory Notice 11-40.

Additionally, purchases and sales of the underlying TRACE-Eligible Securities in order to track the performance of an instrument such as an ETF, without actually creating the instrument, are reportable events and must be reported to TRACE.

As noted in Item 2 of this filing, FINRA has filed the proposed rule change for immediate effectiveness. The implementation date will be 30 days after the date of the filing.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>6</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes that the proposed rule change will clarify members' obligations with respect to the reporting of transfers of TRACE-Eligible Securities to create or redeem instruments such as ETFs under the Rule 6700 Series. In addition, the proposed rule change is consistent with an exclusion for such transfers in equity securities incorporated in FINRA equity trade reporting rules in 2011.

### B. Self-Regulatory Organization's Statement on Burden on Competition

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

### C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition;

---

<sup>6</sup> 15 U.S.C. 78q-3(b)(6).

and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act<sup>7</sup> and Rule 19b-4(f)(6) thereunder.<sup>8</sup>

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

##### Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2012-034 on the subject line.

##### Paper Comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

---

<sup>7</sup> 15 U.S.C. 78s(b)(3)(A).

<sup>8</sup> 17 CFR 240.19b-4(f)(6).

All submissions should refer to File Number SR-FINRA-2012-034. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer

to File Number SR-FINRA-2012-034 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>9</sup>

Kevin M. O'Neill  
Deputy Secretary

[FR Doc. 2012-17444 Filed 07/25/2012 at 8:45 am; Publication Date: 07/26/2012]

---

<sup>9</sup> 17 CFR 200.30-3(a)(12).