

NRS CONFERENCE  
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THE CUTTING EDGE:

REGULATORY FOCUS ON BROKER-DEALER  
TRADING PRACTICES

David M. Sobel, Esq.  
Abel/Noser Corp.  
[dsobel@abelnoser.com](mailto:dsobel@abelnoser.com)

Beth D. Kiesewetter, Esq.  
Morgan, Lewis & Bockius  
[bkiesewetter@morganlewis.com](mailto:bkiesewetter@morganlewis.com)

John Hewitt, Esq.  
McCarter and English  
[jhewitt@mccarter.com](mailto:jhewitt@mccarter.com)

# DARK POOLS

## Dark Pools

Regulation of Non-Public Trading Interest,  
Exchange Act Release No. 34-60997  
(Nov. 13, 2009)

# Purpose

- The SEC proposes to enhance transparency and promote fairer and more efficient markets.
- Amend the definition of “bid” or “offer” in Rule 600(b)(8) of Regulation NMS to apply explicitly to IOIs.
- Lower the trading volume threshold in Rule 301(b) of Regulation ATS.

# HFT

## High Frequency Trading (HFT)

Concept Release on Equity Market  
Structure, Exchange Act Release No.  
34-61358, (Jan. 14, 2010).

# Purpose

- The Staff seeks to elicit input about whether “the overall use of harmful [high-speed trading] strategies by proprietary firms is sufficiently widespread that [the SEC] should consider a regulatory initiative to address the problem.”

# Purpose

- The SEC reviews the characteristics of HFT and its strategies:
  - “Order anticipation” strategy
  - “Momentum ignition”
  - “Arbitrage”
  - “Passive market making”

# MARKET ACCESS

## Market Access-Rule 15c3-5

Risk Management Controls for Brokers or  
Dealers with Market Access, Exchange  
Act Release No. 34-61379 (Jan. 19,  
2010).

# Purpose

- To stop “unfiltered” or “naked” access to an exchange or ATS, the Commission proposed a rule that would require broker-dealers providing direct access to employ risk management controls and supervisory procedures.
- The Commission wants to prevent potential risks to financial exposures from trading errors

# Purpose

or a rapid series of errors arising from computer or human mistakes that are not under the exclusive control of the broker-dealers.

- Proposed rule requires broker-dealers to employ specific systems and procedural controls relating to financial, regulatory, and other business risks.

# Purpose

- Broker-dealers would need to review these procedures regularly and certify their effectiveness.
- Such procedures would need to be under direct and exclusive control of the broker-dealers providing market access.

# PURPOSE

- Proposed rule applies to broker dealers offering “sponsored” or “direct market” access arrangements to customers and to broker-dealers’ proprietary and general agency trading
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# LARGE TRADE REPORTING

Large Trade Reporting System:

Rule 13h-1

Large Trader Reporting System,  
Exchange Act Release No. 34-61908  
(April 14, 2010).

# Purpose

- Rule 13h-1 would require large traders to file Form 13H with the SEC and obtain a large trader identification number.
- The rule would require this identification number to be provided to each broker-dealer for in order to effect transactions.
- Broker-dealers would need to maintain records and data on large trader's

# Purpose

transactions in NMS securities and provide such data to the SEC (via Electronic blue Sheets system) upon the SEC's request.

- The SEC stated that such “reporting system is necessary because. . . large traders appear to be playing an increasingly prominent role in the securities markets.”

# CIRCUIT BREAKER

## Circuit Breaker-Rule 201

Amendments to Regulation SHO,  
Exchange Act Release No. 34-61595  
(Feb. 26, 2010).

# Purpose

- Rule 201 restricts short selling when a stock has triggered a circuit breaker by experiencing a price decline of at least 10 percent in one day.
- Under this rule, short selling would only be permitted if the price of the security is above the current national bid.

# Purpose

- Designed to preserve investor confidence and promote market efficiency while recognizing that short selling can be beneficial and at the same time have harmful effect on the market.
- Requires trading centers to establish and enforce policies to prevent the execution of a short sale orders at a time when the circuit breaker has been triggered by the 10% trigger level.

# Purpose

There are few exceptions to this rule including: domestic and international arbitrage, syndicate transactions, and risk-less transactions by a broker-dealers provided that the broker-dealer's customer has a net long position.

The rule does not apply to derivative products.

# SHORT SELLING

Short Selling in Connection with a Public Offering-Rule 105

Short Selling in Connection with a Public Offering, Exchange Act Release No. 34-56206 (Aug. 6, 2007).

# Purpose

- Amended Rule 105 prohibits a person from selling short the security that is the subject of an offering while purchasing the offered securities if such short sale occurred during the restricted period.
- There are three exceptions to this rule:
  - Bona Fide Purchase Exception

# Purpose

- Separate Accounts Exception and
- Investment Companies Exception