

# FINANCIAL INFORMATION FORUM

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December 3, 2007

Nancy M. Morris, Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, D.C. 20549-1090

Re: File Number SR-NASD-2005-100

Dear Ms. Morris:

The Financial Information Forum ("FIF") appreciates the opportunity to comment on the above-referenced proposal which would require broker/dealers to disclose additional information to certain investors regarding their transactions in corporate debt securities. The Financial Information Forum is a financial services industry organization formed in 1996 to provide a centralized source of information and an opportunity for collaborative resolution of implementation issues that impact financial technology. Our participants include trading and back-office service bureaus, broker/dealers, market data vendors and exchanges. Various committees of FIF have previously worked closely with regulators and industry utilities on implementation considerations for such projects as Reg NMS, OATS, and Decimalization. We will continue our efforts to provide insight and focus on regulatory and industry initiatives aimed at maintaining fair and efficient markets and supporting straight through processing.

This letter reflects specific concerns identified by FIF's Multi-Client Back Office Committee ("the Committee") with respect to non-institutional customer confirmation requirements for transactions in TRACE-eligible securities, as proposed by the Financial Industry Regulatory Authority, Inc. ("FINRA") under Rule 2231 ("proposed Rule 2231", "proposed Rule", or "the Rule"). In addition to relaying our concerns regarding the practicality of providing certain information, the Committee takes this opportunity to comment on the form, timing and recipient of the provisions described in the proposed Rule. Furthermore, as service providers to the broker/dealers, members of this Committee would be directly engaged in modifying existing systems or building new ones to meet the requirements of this Rule. We will therefore comment on the feasibility and time required to implement the proposed Rule.

## **Background**

FINRA's proposal to enhance confirmation disclosure in corporate debt securities transactions mandates disclosure of certain additional information "in the same manner and at the same time in which a member discloses to the customer information in connection with the transaction pursuant to Rule 10b-10 under the Act." The information proposed that is not currently required under Rule 10b-10 includes:

- TRACE symbol if one has been designated by NASD
- Specific statements describing the brokerage charges
- The lowest assigned credit rating (if the security is rated by an NRSRO to which the member subscribes) and the date of such assignment

- A statement disclosing that price information is publicly available for the security and where the investors can obtain this information at no charge
- Cash flow information including but not limited to Yield to Maturity and certain call information (when not otherwise required under SEC Rule 10b-10), and whether the coupon rate is variable
- Compound Accreted Value for zero coupon bonds

A footnote to the proposed Rule as published in the Federal Register specifically states that “FINRA would not interpret proposed NASD Rule 2231 as requiring members to provide the required supplemental disclosures on the same piece of paper or in the same electronic document ... as that containing the SEC Rule 10b-10 confirmation.” The footnote goes on to explain, “FINRA anticipates that the supplemental disclosures of proposed NASD Rule 2231 and the confirmation disclosures required by SEC Rule 10b-10 would be delivered simultaneously.”<sup>1</sup>

The FIF Multi-Client Back Office Committee believes that to the extent the supplemental disclosures are transaction related and must be supplied to the investor at the same time as the trade confirmation, extensive additional processing is required to produce the supplemental disclosures at the same time the broker/dealer is also generating their trade confirmations.

### **The Confirmation Process**

The structure and capabilities of each broker/dealer or service bureau’s existing systems would dictate the design of customized solutions to meet these new requirements; however, were the proposed Rule 2231 to be approved and implemented as described, we anticipate significant impact to the confirmation process for most of the industry. For the majority of broker/dealers, the production of trade confirmations is a very complex, time critical and high volume process. While many of the disclosures proposed with Rule 2231 are no more difficult or complex than other disclosures required on 10b-10 trade confirmations or to meet MSRB G-15 requirements, some of the supplemental disclosures represent a significant increase in the information required on a trade confirmation. This presents issues with space on the printed confirmation, as well as questionable ability to access accurate information and process in a timely manner.

The production of trade confirmations for corporate bond trades in a broker/dealer’s back office system is more or less integrated with that of other investment products (municipal bonds, government bonds, equities, mutual funds, etc.). Although each product has its own unique confirmation requirements, overall there are more similarities than differences in the confirmation process, and the differences have largely been accommodated in one integrated process. The addition of new requirements for TRACE-eligible securities (which typically represent a relatively small number of daily transactions in comparison to other security types) increases the complexity of the overall trade confirmation production process for the broker/dealer.

### **Data Requirements**

Inconsistencies have been identified in comparing the proposed Rule 2231 to requirements established under SEC Rule 10b-10 and MSRB Rule G-15. Specifically, the SEC and MSRB have recognized and exempted disclosure of yield-to-maturity information on confirmations for securities in which a yield to maturity calculation would be inaccurate and/or misleading to the investor. These security types include variable rate bonds such as floaters or stepped coupons

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<sup>1</sup> Federal Register/Vol. 72, No.202/Friday, October 19, 2007/Notices; page 59326.

where future interest rates have not been determined, defaulted bonds, and pay-in-kind securities. We request that FINRA re-examine its rules with respect to these security types to ensure that the calculations required are appropriate and consistent with existing regulations.

The ability to provide the suggested supplemental data on an expanded trade confirmation first requires that the information be collected, scrubbed and stored in the database that supports the confirmation process (a.k.a. security master file).<sup>2</sup> The requirements to include the TRACE symbol and the lowest credit rating with the date of its assignment by the designated NRSRO are particularly troublesome to the Committee for reasons described below.

1. There has been a concerted industry effort to establish a standard security identifier (SSI) that is unique and provides a link to securities descriptions and terms and conditions available from numerous information sources. The industry has generally adopted CUSIP in the U.S. to serve this important function. Most front and back office systems have been programmed to leverage the CUSIP standard for all investment products. The Committee views FINRA's requirement to utilize the TRACE symbol as both confusing to the investor and counterproductive to establishing an industry standard security identifier. An explanation from FINRA might clarify this issue; however, the incremental public benefit of using TRACE symbols beyond the benefit served by using CUSIP as the identifier, remains unclear.

Including the TRACE symbol on a confirmation requires the ability to obtain the symbol and add it to a new field in the security master file on a timely basis. This will be problematic in cases where the security has not been previously or recently traded, and is not currently in the security master file. Data sources, access methods and procedures must be established to ensure the information is available on a timely basis, and is accurate.

Prior to, or in conjunction with, publishing its final requirements using TRACE symbols, we would expect FINRA to provide their plan for the distribution of TRACE symbols to broker/dealers and data vendors, for both new and existing issues. Does FINRA anticipate a requirement on underwriters to obtain and distribute TRACE symbols for an upcoming new issue, as they do for CUSIPs today? Potential licensing issues should also be considered as FINRA formulates its plan.

2. The requirement to include the lowest credit rating and date of assignment is problematic for three important reasons: a) there may be more than one rating for a security, given there are multiple NRSROs; b) the date a rating was assigned is not typically provided by the third-party information vendors from whom broker/dealers and service bureaus receive their descriptive information; and, c) not all broker/dealers have subscription agreements with the rating agencies to permit redistribution of ratings information to their clients. More specifically:
  - a) Multiple credit ratings present an issue because an interpretative program would need to be applied at the time the confirmation is being prepared, comparing inconsistent agency ratings scales in order to properly identify the lowest of the ratings and select it for inclusion on the confirmation. This process would add a layer

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<sup>2</sup> In many firms, there may be differences in the data available to the front-office systems that support trading and 15-minute TRACE reporting requirements, versus the data and processes that support confirmation processing.

- of complexity and increase opportunity for error. If FINRA insists that ratings be provided on confirmations, the Committee's preference is that all ratings for that security currently contained in the security master file be displayed, rather than to require that the lowest be specifically selected, although we recognize that this would further exacerbate the confirmation space issue.
- b) Currently, the date a rating was assigned is a field that is not likely to be included or maintained in a security master file. Even if this field were to be added, it is unlikely that the frequently-used information vendors would be able to provide accurate data to populate this field in the security master. Additionally, the security master file will reflect the ratings most recently applied to the database, not necessarily the most recent ratings assigned. While front-office trading systems typically provide access to real-time information including new ratings assignments and changes, there is most often a lag in the batch processing of ratings updates to the databases that support the confirmation process.
  - c) Not all broker/dealers have subscription agreements in place with ratings agencies to permit access to this information or to allow it to be redistributed to their clients. From the multi-client service bureau perspective, an additional step in the confirmation process would be required to determine for which agencies, if any, the broker/dealer for whom the confirmation is being produced is authorized to provide ratings to their clients.

### **Confirmation Recipient**

FINRA's Rule 2231 is aimed at supplementing the information made available to non-institutional (retail) investors to provide additional knowledge about their investments. The Rule as proposed differentiates between disclosures that must be made available to non-institutional investors versus institutional investors, and stipulates that the institutional status of an account must have been determined within the past twelve months. We believe that once an account has been established as an "institutional account" in accordance with a set of firm-specific procedures, it is unnecessary to review the status of that account annually for these purposes. Furthermore, until an account has been determined to be an institutional account, it would be treated as a non-institutional account, and subject to the provisions of proposed Rule 2231. We request that the reference to time ("within the last twelve months") be eliminated from the Rule, and allow treatment of the account for confirmation purposes to be a "principles-based" approach.

### **Form**

The requirements proposed in Rule 2231 to add data and provide lengthy references to availability of additional information upon written request, present significant space issues on an already-packed confirmation document. The addition of the language proposed by this Rule will require some broker/dealer firms to undergo major redesigns of their print confirmation formats. This could also have an adverse impact on the on-going costs of printing, mail preparation and postage.

Rather than require that disclosures be provided "in the same manner and at the same time as the SEC Rule 10b-10 confirmation", our Committee suggests that security-specific information could be made available on a public website, while information that is transaction-specific would continue to be provided on the confirmation (in either print or electronic form according to the investor's preference), and remain the responsibility of the broker/dealer. For instance, on their publicly accessible website [www.bondinfo.com](http://www.bondinfo.com), FINRA could provide a cross-reference of CUSIP to TRACE symbols, as well as additional descriptive information such as the lowest rating and assignment date for all TRACE-eligible securities. This would ensure that investors

have access to consistent information. In addition, this would improve the timeliness of the descriptive information available to investors about the securities they have purchased. The current process of a printed confirmation mailed on T+1 (the day after trade date) and received several days later, is certainly less desirable than providing an investor with immediate access to current information about the specific security they have traded or similar transactions. The added benefit to the investor is that they would not receive static data that may be stale, but would have easy access to current information on an ongoing basis.

### **Implementation Requirements**

We do not dispute the value of much of the supplemental disclosures required under proposed Rule 2231; however, we would like FINRA to recognize the impact of adding these requirements to an already complex and time critical process for broker/dealers. As an example, calculation of the Compound Accreted Value for zero coupon bonds will require extensive calculations that are not currently performed as part of the confirmation process for TRACE-eligible securities. These new capabilities will require a substantial development and testing effort. Sufficient time must be allowed to avoid errors and not adversely impact either broker/dealers or investors.

In summary, even the most modest changes proposed by FINRA Rule 2231 will result in modifications to complex back office processes that will require significant testing of new functionality, as well as regression testing of existing features and the overall process. To successfully complete such a project would take a minimum of six months from the date that final requirements are published. Concurrently, broker/dealers (and we as their service vendors) are engaged in preparing for numerous other regulatory mandates such as trade reporting; hence, resources are stretched for the foreseeable future. With this mind, we respectfully request that FINRA allow as much time as possible for programming and testing prior to the effective date of the Rule. In addition, we ask that the schedule be arranged to avoid implementation between the dates of November 1<sup>st</sup> and January 31<sup>st</sup>, as many firms have "system freezes" during those periods.

Thank you again for the opportunity to share our experience and concerns regarding this significant proposal. If you wish to discuss any aspect of these comments in greater detail, our Committee will be happy to participate in follow-up meetings.

Respectfully submitted,



Manisha Kimmel  
Executive Director, Financial Information Forum  
on behalf of the FIF Multi-Client Back Office Working Group