



March 22, 2010

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE.
Washington, DC 20549-1090

Re: [Release No. 34-61566; File No. SR-FINRA-2009-065] Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1 Thereto, To Require the Reporting of Transactions in Asset-Backed Securities to TRACE

Dear Ms. Murphy,

The Securities Industry and Financial Markets Association (SIFMA¹) is pleased to respond to this request for comments on the SEC's approval of SR-FINRA-2009-065, as amended. SIFMA believes that the restoration of securitized products markets is an essential and necessary component of any broad-based economic recovery, and is key to the return of more normal levels of credit availability that are important contributors to economic growth. Because transparency within the structured finance products and markets is a necessary component of such recovery, SIFMA will continue to suggest ways to improve transparency with those markets.

We note with encouragement several of the changes made to the initial proposal embodied by Amendment No. 1, such as FINRA's decision to maintain reference data that will eliminate the need for dealers to separately report factor information, and the allowance for reporting of generic TBA CUSIPs.² We believe these changes, along with other positive adjustments to the proposal, will serve to increase the efficiency of the TRACE system and the reporting processes of FINRA member broker-dealers, and decrease their initial set-up costs. Therefore, SIFMA is broadly supportive of the changes to the initial proposal described in Amendment No. 1.

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 www.sifma.org.

² Amendment No. 1 is available here:

<http://www.finra.org/web/groups/industry/@ip/@reg/@rulfil/documents/rulefilings/p120749.pdf>

In this letter, we will provide additional feedback on certain of the changes discussed in Amendment No. 1, and will also discuss important issues that we believe have not been appropriately addressed to this point.³

We would also like to use this letter as an opportunity to reiterate how important it is that FINRA's TRACE implementation policies and procedures account for the diversity of the mortgage- and asset-backed securities markets. For example, although there are a number of participants in the agency debentures markets, the securities and trading practices for agency debentures are relatively homogeneous when compared to asset-backed securities markets as defined in the rule proposal.

The securitized products "market" actually consists of numerous distinct "sub-markets," each of which is very large in scope and contains separate and distinct origination, trading, and settlement practices. While certain sub-markets, such as secondary trading markets for previously issued private label MBS and ABS are relatively similar to the markets for corporate debt, other sub-markets – such as TBA trading of agency MBS, new issue private label MBS and new issue ABS – are different from each other and also vastly different from any market for which TRACE has been previously implemented. Because these differences can present challenges and uncertainty regarding TRACE reporting, SIFMA believes that thoughtful consideration should be given to the implementation of TRACE in each of these sub-markets, and careful guidance should be issued in order to maximize transparency.

In the comments that follow, we outline a number of significant areas of uncertainty together with actions on the part of FINRA that are needed with respect Amendment No.1 to SR-FINRA-2009-065. We also encourage FINRA to maintain and enhance the productive and beneficial dialog with broker-dealers that was initiated in the lead up to the agency debenture implementation.

1. FINRA Should Prioritize the Development of a More Flexible System for Reporting Trade Modifications

FINRA noted in its response to comments on the initial rule proposal that "generally, amended transaction reports will not be required when modifications occur relating to delivery of assets/collateral and/or settlement of a transaction."⁴ SIFMA believes this is an appropriate policy, given that amendments to trades for immaterial changes related to settlement would only serve to incrementally increase operational costs without providing meaningful new information.

SIFMA recommends that FINRA publish guidance with more specificity as to when a trade should be amended, and when a trade need not be amended. For example, trade assignments are

³ Please see SIFMA's previous letter on this topic, available here: <http://www.sifma.org/legislative/pdf/ResponseFinraTRACE1118209.pdf>

⁴ FINRA response to comments at 8.

a common practice in the market for TBA trading of agency MBS. These represent the assignment of settlement obligations of a given trade from one counterparty to another, and accordingly would seem to fall within the scope of the policy outlined by FINRA that is quoted above. However, in many instances a customer will assign a trade settlement to a broker-dealer. Thus, on the initial transaction report, the contra-party identifier would be a “C” for a customer trade. When the assignment is executed, the counterparty would become a broker-dealer presumably with its own MPID. Members generally believe that FINRA’s policy mandates resubmission if any initial transaction report information changes – however, changes such as the one noted above relate solely to a settlement obligation and are not material to trade price, volume, or other terms. It is unclear if such trade assignments would require resubmission of transaction information – we believe they should not. If FINRA were to require resubmission, the transaction report, as revised, should not be considered to be late. SIFMA recommends that FINRA provide guidance on this point.

SIFMA also notes FINRA’s statement in its response to comments that more general issues regarding trade modifications and cancellations and corrections of previously submitted data are “not relevant to the proposed rule change”.⁵ We do not agree with this conclusion. Given the significant, massive increase in volumes that will attend MBS/ABS reporting, issues around modifications of previously submitted transaction information will strike at the core efficiency, cost and operational burdens of complying with the requirements of TRACE reporting. For broker-dealers, these modification issues will likely result in additional costs and regulatory scrutiny related to accommodating their clients’ requests for trade modifications. Furthermore, FINRA will need to be able to efficiently and accurately sift through trade reports in numbers an order of magnitude beyond those which are currently reported. While these issues are likely to be most acute for MBS/ABS due to volumes, they exist for all TRACE-eligible securities. SIFMA strongly believes it should be a primary goal for FINRA to develop a more modern and flexible system, similar in spirit to that of the MSRB, which will allow dealers to correct trade reports.

We reiterate our previous comments on this point:

“We agree that changes to material terms of a trade such as the price, size, or whether it was a buy or sell should require a change to the original TRACE submission. However, to echo SIFMA’s earlier comments to FINRA on trade modifications, we suggest that FINRA should follow the MSRB’s approach to trade modifications where changes to several fields in customer transactions are separately classified as “amendments” rather than “late trades” and are tracked separately for report card purposes and regulatory analysis.”⁶

SIFMA members strongly believe that TRACE reporting should not negatively impact common, longstanding and beneficial market practices (such as trade assignments) that serve to promote the efficiency of ABS and MBS markets. TRACE rules and policies should recognize the

⁵ FINRA response to comments, at 9.

⁶ SIFMA November 18, 2009 comment letter, at 8.

differences between adjustments to trades that are part of the normal course of business and facilitate customer requests, and those that are truly late.

2. Guidance is needed regarding Issues that Arise in the MBS/ABS Issuance Process

In our previous letter, we noted the significant number of trades in asset-backed securities that are executed before CUSIP information is known. FINRA has indicated to SIFMA that guidance is being developed regarding the process for the submission of trades to TRACE when CUSIPs are not known, including guidance around the issues of when trades should be submitted, and also regarding the process to obtain an ID from FINRA when a CUSIP is not available⁷. For the reasons that follow, SIFMA strongly supports an outcome whereby transactions are reported to TRACE only when a deal's structure has been finalized and CUSIPs issued – in other words, a single report for each trade related to the issuance of a new structure.

In the issuance process for MBS, trades often occur during the process of structuring the transaction. Because these securitization transactions are, generally speaking, customized to investors' needs, the transactions are very commonly amended (at the request of the investors) in order to restructure a position, change allocations, or otherwise change the investors' investment. If transactions are TRACE reportable prior to finalization of the structure, the result will be a large number of amendments to previously reported transactions. Such multiple amendments will not enhance price transparency or FINRA's ability to supervise these markets.

Similarly, in the issuance process for syndicated ABS (as opposed to private label MBS, which generally do not use a syndicate), investors will often designate one syndicate member as the party who will deliver bonds to the investor from a number of other syndicate members. Specifically, investors commonly purchase bonds from multiple syndicate members but desire to take delivery of all purchased bonds from a single counterparty in order to decrease settlement risk (or for some other reason). To facilitate the wishes of the investor, the other syndicate members will enter into transactions with this "designated" syndicate member so that the designated dealer may deliver the investor's entire allotment. SIFMA members believe that such inter-dealer transactions should be added as an exemption from reporting requirements in Rule 6730(e), as they do not provide meaningful price information – they are merely a means to fulfill the settlement-related request of an investor.

3. Settlement Date Reporting Changes Proposed in Amendment No. 1 are Helpful, Yet Redundant

In Amendment No. 1, FINRA proposes that dealers "report the actual date of settlement and indicate if the transaction will or will not settle "regular way"". SIFMA requested the ability of dealers to report actual settlement dates in our previous letter. We noted that "this would provide

⁷ There are implementation questions around using and creating new street-wide identifiers that require some analysis on the part of broker-dealers, therefore it is preferable for this guidance to be issued at the same time as the broader technical specifications.

for a more flexible system, be easier for dealers to implement, and result in fewer compliance issues (as opposed to requiring the derivation of number of days until settlement and resulting disputes over treatment of holidays, etc). Furthermore, this would provide FINRA with maximally granular information regarding transactions in the most direct manner.”⁸ We are pleased that FINRA was amenable to this change; however, we have concerns regarding how it is being implemented.

The amended rule proposal would require dealers to report both the actual settlement date *and* whether or not the trade was regular way. Given that the reporting of actual settlement dates would allow FINRA to derive whether or not a trade was regular way, it is unclear why FINRA still intends to require dealers to provide this information. Requiring both settlement date and “regular way” or “not regular way” will increase complexity in settlement date reporting for firms and could potentially result in further discrepancies, as reporting “regular way” or “not regular way” requires calculation by reporting systems. Therefore it introduces a potential for unintentional and immaterial mistakes that could impact broker-dealers significantly while not providing a substantial offsetting benefit to FINRA. We believe this requirement should be revised to require only the submission of the settlement date. This would be consistent with FINRA’s previous change in eliminating need for each firm to report yield on trade reports; instead, FINRA uses data provided and has a standard calculation of yield. Furthermore, SIFMA believes that this method of reporting trade settlement dates should be applied globally across all TRACE-eligible products.

4. Improvements Are Needed to the Issue Master File Distribution Process

We reiterate the points made in our previous letters on the topic of the Issue Master File distribution process. SIFMA members believe that a more robust process for the dissemination of intra-day updates is needed, and recommend that FINRA work toward a system for the Issue Master that is capable of pushing real-time notifications of additions of each new security, and updates to existing securities, to FINRA-member broker-dealers. We recognize that this is a long-term project and is not something that will be implemented in the very near future. Therefore, in the very near term we recommend that FINRA, at minimum, implement improvements to the Issue Master File distribution process that result in the production of comprehensive “difference” files that allow users to know what has changed from the previous version without needing to re-download all of the data. The current difference files that are produced every 30 minutes throughout the day are not complete because they do not reflect all changes made to existing securities on the Issue Master. We believe this is a reasonable request that will significantly ease the current burden on broker-dealers, who now must re-download the entire Issue Master to understand the totality of changes to securities. Given that over one million ABS/MBS CUSIPs will be added to the Issue Master File upon implementation, this is very important, as the Issue Master will grow exponentially. Because of the foregoing reasons, if FINRA plans to continue to require securities to appear on its Issue Master file before they are

⁸ Id. at 11.

admitted for reporting, FINRA should improve and make more real-time the ability of dealers to know what securities are, and are not, on the master.

5. Technical Specifications and Implementation

SIFMA encourages FINRA to publish technical specifications for the TRACE reporting of MBS and ABS as soon as possible. From the perspective of a broker-dealer, the implementation can really only begin with technical specifications in hand.

Furthermore, SIFMA reiterates points made in the last letter regarding the need for an adequate test environment and period of time in which to test. SIFMA members recommend that the test environment mimic, as closely as possible, the production environment. Therefore, the test security database should include the entire CUSIP range for these products. Furthermore, dealers should have the opportunity to perform volume testing, as well as testing of the new-issue set up process. Members also believe that due to the added complexity of the MBS/ABS implementation, the period of time that dealers are able to test free of charge should be extended. Finally, many members have raised an issue with previous TRACE test environments in that dealers do not have enough visibility into the test transactions they are submitting. In other words, dealers do not always know if they have submitted trades correctly, and at times it is difficult to discern what errors they created, as the process for reporting on the test transactions is somewhat cumbersome.

Given the significantly increased complexity of reporting and volume of trades in securitized products (specifically, Agency MBS), we recommend that FINRA institute a brief grace period at the outset of the effective period, during which for a period of time, dealers who act in good faith are not penalized for errors or omissions in their trade reports. Due to the nature (and volume) of TBA trading of Agency MBS, we believe this period should cover an entire settlement cycle to be meaningful. The vast majority of TBA trades will take place around the period of time comprising the Class A settlement day, which is usually in the beginning of the month. At a minimum, this grace period should include the first Class A settlement day and a period of days prior to and following that day.

6. New Issue Notification and Set-Up Process

SIFMA members appreciate the efforts made by FINRA in the context of Agency debentures to quickly remedy issues that arose during the week of implementation of reporting for those securities. However, we note that these issues will likely become more common given the massive increase in volume that is expected with the implementation of TRACE for MBS/ABS.

Due to the manual nature of the process, delays sometimes occur in FINRA's set up process for new issue securities even when the dealer has presented FINRA with all relevant information for a transaction. In such cases, trades are sometimes rejected by the TRACE system because it does not yet recognize the CUSIP or other identifier. FINRA has stated that the absence of a security from the issue master list is *not* determinative of whether or not it is required to be reported;

logically, it follows that securities that are not on the issue master indeed are likely to require reporting. In order to implement the most efficient process to accommodate this, FINRA should not simply reject transactions in securities that do not appear on the Issue Master; rather, they should be flagged and set aside for review by FINRA staff. If a submitted CUSIP passes a validity check, the CUSIP should be accepted. We understand that FINRA has expressed concern regarding dissemination (in the corporate and agency debenture markets) of trades with CUSIPs that have not been verified to FINRA's comfort; this is understandable, but FINRA could organize a process to verify CUSIPs before information is disseminated.

Furthermore, SIFMA members believe that if dealers attempt to manually re-submit the trade after FINRA sets the security up in the Issue Master and it is accepted, FINRA should not count these trade reports as "late submissions" because that reporting delay was caused by FINRA's delay in setting up the issue. FINRA has advised that such reports would be excluded from regulatory action if members notify FINRA. We do not believe that members should bear the burden of reporting these issues to FINRA; rather, FINRA should track and exclude these issues automatically. Consequently, SIFMA dealer members recommend that FINRA continue to enhance their current efforts to expedite set-up times to minimize such rejections, and encourage FINRA to undertake a dialog with dealers to determine how this can be most effectively implemented. In the interim, the methodology for evaluating compliance should exempt trades re-submitted in connection with such trade rejections from firms' late reporting statistics.

7. TRACE Fee Structure Should Be Reviewed and Adjusted

We note that FINRA has rejected SIFMA's requests to review and revise the TRACE fee structure when TRACE reporting is implemented for MBS and ABS. We are disappointed by this rejection as our members feel strongly that the total costs of implementation and reporting of MBS and ABS trades to TRACE will be material and significant to even the largest of our member firms. We quote from our previous letter:

Some of our dealer members have undertaken preliminary analyses of trading volumes and indicated that reporting volumes may double with the implementation of TRACE reporting for Agency debentures and primary market transactions in March 2010. As a point of comparison to other markets for which TRACE reporting is or will be required, according to data published by the Federal Reserve Bank of New York, primary dealers reported 2009 year-to-date average daily trading volumes for MBS that were approximately 2.2 times higher than those of corporate debt, and higher than those of corporate and Federal Agency debt combined⁹. Clearly the implementation of TRACE reporting for [securitized products] will cause a further, major increase in reporting volumes and this should be reflected in the implementation of this process.

In other words, based on numbers such as those noted above, revenue from TRACE reporting is likely to increase quite significantly. The costs for many of our dealer members, even leaving aside implementation costs (which will also be significant), may therefore more than double depending on trading activity. This cost increase will be especially acute for interdealer brokers.

⁹ "Year-to-date Market Share Data of Primary Dealer Transactions", Federal Reserve Bank of New York. Data covers 1/7/2009 through 9/30/2009. <<http://www.newyorkfed.org/markets/statrel.html>>

This will vary on a firm by firm basis, but the overwhelming point is that trading volumes in MBS and ABS are significantly higher than all other fixed income products aside from Treasuries – in other word volume from MBS/ABS will dwarf volume from all other TRACE-eligible securities.

We understand that FINRA will incur significant costs as it develops the capacity to receive information on MBS and ABS trades. In fact, SIFMA strongly encourages FINRA to invest in new technology to implement TRACE reporting for MBS and ABS and modernize the TRACE infrastructure, and also to make investments to upgrade the infrastructure that supports the TRACE reporting systems generally, in order to create a more robust and reliable environment. We also understand that FINRA is likely to incur greater costs regarding oversight, examinations, and surveillance. However, SIFMA believes that the revenue generated by MBS and ABS trade reporting will far exceed of these costs, and the fee structure therefore must be reviewed and adjusted to take into account the massive increase in trade reports that will result from MBS and ABS trade reporting. SIFMA members believe this review of the fee structure should come before, not after, reporting for MBS and ABS is implemented.

We commend FINRA on their outreach to the dealer community in the time leading up to the implementation of TRACE reporting for Agency debentures and we encourage FINRA to maintain this open attitude towards member firms vis-à-vis conference calls, individual meetings, and dialogue with SIFMA. SIFMA stands ready to assist FINRA with maintaining an open and productive dialog as we progress toward implementation for MBS and ABS TRACE reporting.

Please do not hesitate to contact Chris Killian on my staff at 212-313-1126 or ckillian@sifma.org with any questions, or for more information on any issue related to this letter.

Sincerely,



Randolph C. Snook

Senior Managing Director and Executive Vice President
Securities Industry and Financial Markets Association