



REGIONAL
BOND DEALERS
ASSOCIATION

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CHAIRMAN'S
CORRESPONDENCE UNIT

March 8, 2010

The Honorable Ben S. Bernanke
Chairman
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

Mr. Richard G. Ketchum
Chairman and Chief Executive Officer
Financial Industry Regulatory Authority
1735 K Street, NW
Washington, DC 20006

RE: Exclusion of Bank Dealers from TRACE Expansion

Dear Chairman Bernanke and Mr. Ketchum:

The Regional Bond Dealers Association ("RBDA") is concerned that the exclusion of bank dealers from the purview of the TRACE reporting requirements that are now applicable to agency debt securities will materially undermine the ability of the Rule 6710 amendments to achieve the stated goals of the Financial Industry Regulatory Authority ("FINRA"). While we applaud FINRA's commitment to market transparency, this exclusion of a large class of agency debt market participants will in fact compromise the reliability of the information that is ultimately reported pursuant to Rule 6710 and will create a material competitive advantage for bank dealers at the expense of both broker-dealers and the other market participants FINRA intends to protect. We therefore urge the Board of Governors of the Federal Reserve System (the "Board") to require a corresponding degree of transparency with respect to bank dealers' trades in agency debt securities, and we urge FINRA to suspend the Rule 6710 amendments until the agency debt pricing information made available to the market is no longer inherently skewed.

FINRA has stated that the amendments were prompted by the fact that there has historically been "no centralized public dissemination of information regarding transactions in Agency Debt Securities," and has maintained that providing "comprehensive" post-trade information with respect to agency debt securities will "assist in price discovery and valuation processes for all market participants and provide retail investors access to price information currently not readily available to non-professionals."¹ However, the reliability of the information provided to market

¹ Letter to Elizabeth M. Murphy, Secretary, SEC, from Sharon Zackula, Associate VP and Associate General

participants is crucial to the success of such valuation processes; in particular, the post-trade information provided must be representative of the industry as a whole. Clearly, therefore, an exemption of bank dealers from any corresponding reporting requirements will distort the pricing information that is made available to the market. In this regard, it should be noted, for example, that the top fifteen U.S. debt and equity underwriters from 2008 are all bank-affiliated.²

While, through Regulation R,³ the Board and the Securities Exchange Commission (the “SEC”) have begun to address the question of when a bank’s securities activities will require it to register with the SEC as a broker, FINRA’s by-laws themselves specifically exclude banks from the definitions of “broker” and “dealer” as those terms are used therein,⁴ and therefore ultimately exclude bank dealers from the scope of the TRACE amendments. Consequently, unless the Board acts to ensure that banks’ trades in agency debt securities are reported to the market in a manner that is consistent with—in terms of both frequency and detail—the reporting now required to be made by broker-dealers, the reliability of the trade information that is provided to market participants will be significantly undermined. In fact, RBDA members across the country have already observed a clear market reaction to this regulatory imbalance: On the very day on which amended Rule 6710 went into effect, our members learned of a number of financial institutions that are actively taking steps to ensure that agency debt security trades are handled by entities which, because of their status as banks, are beyond the reach of FINRA’s rules. There is no reason to believe that such counterproductive activity will not continue to spread throughout the industry for as long as the incentive that is created by this imbalance is allowed to persist; and those market participants who effect the largest number of trades in agency debt securities will clearly have the greatest incentive to follow suit.

Moreover, in the absence of any corresponding bank dealer regulation, the application of amended Rule 6710 to broker-dealers creates an uneven playing field between the two classes of market participants. To become compliant with the new TRACE reporting requirements, broker-dealers must develop new technological and administrative reporting systems, pay reporting fees and otherwise fund ongoing compliance. These costs, which can be significant for firms that are active in the agency securities market, will not be incurred by similarly active bank dealers. Moreover, while bank dealers will now necessarily have access to broker-dealers’ trading and pricing activity, broker-dealers—like the rest of the market—will have no access to bank dealers’ post-trade information, thereby putting broker-dealers’ trade desks, and their clients, at a clear disadvantage.

In light of the foregoing, and given that FINRA’s stated purpose was to provide the market with comprehensive post-trade information on which agency debt market participants could base their

Counsel of the Financial Industry Regulatory Authority, dated August 26, 2009.

² Investment Dealers Digest (January 12, 2009): 1) JPMorgan, 2) Barclays Capital, 3) Citi, 4) Banc of America Securities, 5) Merrill Lynch, 6) Goldman Sachs, 7) Deutsche Bank, 8) Morgan Stanley, 9) Credit Suisse, 10) UBS, 11) RBS, 12) HSBC Holdings, 13) Wachovia, 14) First Horizon National, 15) RBC Capital Markets.

³ 12 C.F.R. Part 218 (2009).

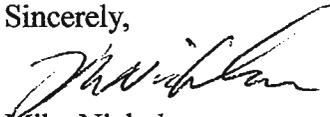
⁴ FINRA By-Laws, Article I.

Hon. Ben S. Bernanke
Mr. Richard Ketchum
March 8, 2010
Page 3

price discovery and valuation processes, we recommend suspending the Rule 6710 amendments until the regulatory imbalance described above—and the resulting counterproductive incentive structure—have been sufficiently resolved. To do otherwise would simply ensure that the very market participants that FINRA hoped to benefit will instead be provided with increasingly misleading pricing information regarding agency debt securities.

Thank you for considering our concerns. Please do not hesitate to call if you have any questions or would like to discuss this matter further.

Sincerely,



Mike Nicholas
Chief Executive Officer

Cc: Chairman Christopher J. Dodd, U.S. Senate Cmtee. on Banking, Housing & Urban Affairs
Mr. John C. Dugan, Comptroller of the Currency
Chairman Barney Frank, U.S. House Cmtee. on Financial Services
Chairman Mary L. Schapiro, U.S. Securities and Exchange Commission