Secretary, Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

February 10, 2016

Thank you for the opportunity to again comment on FINRA's proposed amendments to Rule 4210. As I have previously stated, the Commission should reject the proposal in its entirety. I am convinced that (1) FINRA does not possess the statutory authority to regulate exempt securities in the manner proposed in the amendments to Rule 4210, (2) the inclusion of specified pools and GSE Sponsored CMOs in the definition of "Covered Agency Securities" has not been thoroughly vetted and (3) the proposal is anti-competitive on a number of levels.

In my previous comment letter I stated that I believed that Section 15A (b) 6 of the Exchange Act did not supersede the authority of Congress to exempt activity from that authority. FINRA has responded that 15A (b) 6 does grant them the power to adopt the proposed amendments. My point was not that FINRA does not believe it possesses the authority: my point was that Congress does not think so. I questioned the logic of believing that Congress did not intend to protect exempt securities from margin requirements while extending the margin requirement protections of Section 7(g) to non-exempt securities. In the 1983 report of the Senate Committee on Banking, Housing and Urban Affairs on the Secondary Mortgage Market Enhancement Act, the Committee addressed the need to adjust margin requirements for mortgage related securities "because of the unique nature of the secondary mortgage market." The end result of this and other analysis became what is now Section 7 (g) of the Exchange Act. Section 7 (g) applies to non-exempt mortgage related securities. Why would Congress not include exempt securities within the definition of "mortgage related securities"? Because Congress believed that the exemptions that already existed in Section 7 addressed exempt securities. From page 8 of the report (where the margin issue is addressed): "It should be noted that government-backed mortgages are exempt from these rules now." Such language should create a rebuttable presumption that Congress did not intend to grant FINRA the power to adopt margin requirements for exempt securities.

If one accepts the argument that Congress unintentionally, but nevertheless effectively granted FINRA the authority to require margin on transactions in exempt securities, the amendments still fail to meet the requirements of 15A (b) 6. FINRA has not claimed that markets for "Covered Agency Securities" are being manipulated. FINRA has claimed, but has not demonstrated, that including specified pools and CMOs within the definition of "Covered Agency Securities" protects investors or the public interest. The proposal injures and does not promote just and equitable trading practices.

During this entire process, it has been noted that the TBA market is not margined like "other contract" markets, that it is a $5 trillion market, there is little if any retail participation and that the TBA market represents systemic risk. All of these things are true. The problem is that FINRA is not proposing to regulate only the TBA market. FINRA is including specified MBS pools and CMOs in its definition of

"Covered Agency Securities", and the above statements do not apply to specified MBS pools and CMOs. Furthermore, after including specified MBS pools and CMOs in its definition of "Covered Agency Securities", FINRA proceeds to analyze the economic effects of the proposal based upon the TBA market alone, not upon the specified MBS pool and CMO market. "Covered Agency Securities" are then referred to generically as TBAs. It is misleading to refer to specified pool and CMO activity as TBA activity. This is rather akin to someone, after being confronted with the problem of dogs chasing cars, proposes a rule requiring all "animals" to remain fenced or inside; expands the definition of covered "animals" to include cats (at the request of the doctor that lives at the end of the block) and then analyzes the proposal based upon the behavior of dogs alone, stating that for convenience all "animals" will be referred to as dogs. This might not be so terrible, but for the fact that cats do not generally chase cars and cats are a lot harder to keep inside a fence. FINRA piled the specified pool and CMO market in with the TBA market in their analysis and created a distorted view of the necessity of including specified pools and CMOs in the proposal. Yet, the specified pool and CMO market is where most FINRA members will be affected.

In FINRA's response to comments it was noted that staff at the FRBNY was insistent that FINRA not exempt from the proposed requirements MBS pool and CMO trades that settle on the first day good settlement figures are available. I have yet to see the proposal that would require Fed member dealer banks to comply with the same requirements. Why is it that FINRA is imposing requirements on its members based upon representations made by Fed staffers that are not recommending that the same requirements be imposed on Fed member banks?

My rudimentary analysis in 2014 (referred to in my original comment letter) revealed that (1) the TBA market is 7 times the size of the specified pool and CMO market (2) the specified pool and CMO market are investment markets and not "contract" or financing markets, (3) retail is a significant participant in the specified pool and CMO market (51 percent of the trades are between $0 and $100,000 face amount) and (4) the specified pool and CMO markets do not represent systemic risk (a 100 basis point move in 10 business days would create a system wide potential loss of $4 billion if 25 percent of the volume failed to settle). Where is the analysis from FINRA that addresses the markets individually? The TBA and specified markets are different in nature and size: regulation of the two should take these matters into account.

The proposed amendments are anti-competitive on a number of levels. FINRA argues that requiring FINRA members to margin "Covered Agency Securities" somehow prevents a competitive imbalance between dealer banks that voluntarily observe TMPG recommended practices and FINRA dealers that choose not to. If the proposed amendments are adopted, dealer banks that choose to observe TMPG recommended practices will still be at a competitive disadvantage to those dealer banks that choose not to follow TMPG recommended practices. FINRA members will be the only parties required to impose margin requirements on transactions in "Covered Agency Securities". Even the bank dealers that are currently observing TMPG recommendations may choose not to in the future. FINRA claims that there is a competitive imbalance represented by one set of dealers voluntarily observing standards that others are not, but it is somehow not anti-competitive to *require* one set of dealers to observe standards that do not apply to others? The proposal also places a disproportionate burden on smaller dealers. It will be impossible to operate without a margin department under the proposal as written. Smaller dealers will find it considerably more burdensome to create a margin department at costs of hundreds of thousands of dollars compared to larger dealers that have already invested millions in the software and personnel that currently staff their margin departments. The marginal cost of adding even one person will weigh more heavily upon small dealers. Furthermore, these dealers will be creating systems and departments to monitor transactions that will rarely result in the movement of money. FINRA freely admits that few accounts would be required to post margin under the proposal. Trade analysis at our firm indicates that the current proposal would not have resulted in having to collect margin on specified pool or CMO transactions on more than a couple of occasions over the last year. Despite this, the proposal would require us to obtain executed MSFTAs from our clients and create a margin monitoring protocol related to specified pool and CMO transactions, most of which settle on the first day good settlement figures are available. There will be dealers that exit the arena rather than implement the protocol required by the proposal. This is unlikely to have much effect on liquidity, but will affect competition, and these are dealers that are all but non-existent in the actual TBA market.

Then there is what may be the crux of the matter. Large institutional clients will be hesitant to execute MSFTAs with numerous small broker-dealers, whereas today many can present large institutional clients with ideas related to mortgage backed product. The elimination of smaller dealers as competitors for the business of large institutional clients would certainly benefit larger dealers at the expense of smaller ones.

Most of these arguments have already been made and FINRA determined that the costs do not outweigh the benefits of "TBA" margining. This line of reasoning also ignores the fact that many of the smaller dealers affected by the proposal do not participate in the actual TBA market. The only way the math works is if one lumps the specified pool and CMO market in with the TBA market. This is patently unfair to those dealers that do not routinely participate in the TBA market.

It is understood that the massive dollar roll TBA market represents potential systemic risk, and that regulators are right to take action to reduce system wide exposure to that risk. However, FINRA does not have to amend Rule 4210 to address this issue. If the transaction is truly a financing, that transaction should not be executed in a cash account. The transaction could be executed in the margin account and subject to the rules that apply to margin accounts.

In summary, Congress has made it clear that Section 15A (b) 6 was not intended to be a back door for regulators to circumvent Section 7, the specified pool and CMO markets do not represent systemic risk and FINRA has not presented any evidence to the contrary, the proposal is anti-competitive on its face and places a proportionately larger burden on smaller dealers and the proposal unnecessarily wreaks havoc on an investment market that is operating on a sound basis. For any one of these reasons, FINRA should be required to withdraw this proposal. At the very least, FINRA should be required to demonstrate the need for the proposal as it relates to the specified pool and CMO market specifically, and not in conjunction with the TBA market. Thank you again for the opportunity to comment on the proposal.

Sincerely,

Chris Melton
Executive Vice President
Coastal Securities